Y4.B22/1:97-53

HOUSING AND URBAN-RURAL RECOVERY ACT OF 1982

COMPLETED
726

ORIGINAL

HEARINGS

BEFORE THE

SUBCOMMITTEE ON
HOUSING AND COMMUNITY DEVELOPMENT

OF THE

COMMITTEE ON
BANKING, FINANCE AND URBAN AFFAIRS
HOUSE OF REPRESENTATIVES

NINETY-SEVENTH CONGRESS

SECOND SESSION

PART 2

MARCH 18 AND 25, 1982

Serial No. 97-53

Printed for the use of the
Committee on Banking, Finance and Urban Affairs

HOUSING AND URBAN-RURAL RECOVERY ACT OF 1982

HEARINGS

BEFORE THE

SUBCOMMITTEE ON HOUSING AND COMMUNITY DEVELOPMENT

OF THE

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
HOUSE OF REPRESENTATIVES

NINETY-SEVENTH CONGRESS

SECOND SESSION

PART 2

MARCH 18 AND 23, 1982

Serial No. 97-53

Printed for the use of the
Committee on Banking, Finance and Urban Affairs

U.S. GOVERNMENT PRINTING OFFICE
94-931 O WASHINGTON : 1982

I

HOUSE COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

FERNAND J. ST GERMAIN, Rhode Island, *Chairman*

HENRY S. REUSS, Wisconsin
HENRY B. GONZALEZ, Texas
JOSEPH G. MINISH, New Jersey
FRANK ANNUNZIO, Illinois
PARREN J. MITCHELL, Maryland
WALTER E. FAUNTROY, District of Columbia
STEPHEN L. NEAL, North Carolina
JERRY M. PATTERSON, California
JAMES J. BLANCHARD, Michigan
CARROLL HUBBARD, Jr., Kentucky
JOHN J. LaFALCE, New York
DAVID W. EVANS, Indiana
NORMAN E. D'AMOURS, New Hampshire
STANLEY N. LUNDINE, New York
MARY ROSE OAKAR, Ohio
JIM MATTOX, Texas
BRUCE F. VENTO, Minnesota
DOUG BARNARD, Jr., Georgia
ROBERT GARCIA, New York
MIKE LOWRY, Washington
CHARLES E. SCHUMER, New York
BARNEY FRANK, Massachusetts
BILL PATMAN, Texas
WILLIAM J. COYNE, Pennsylvania
STENY H. HOYER, Maryland

J. WILLIAM STANTON, Ohio
CHALMERS P. WYLIE, Ohio
STEWART B. McKINNEY, Connecticut
GEORGE HANSEN, Idaho
JIM LEACH, Iowa
THOMAS B. EVANS, Jr., Delaware
RON PAUL, Texas
ED BETHUNE, Arkansas
NORMAN D. SHUMWAY, California
STAN PARRIS, Virginia
ED WEBER, Ohio
BILL McCOLLUM, Florida
GREGORY W. CARMAN, New York
GEORGE C. WORTLEY, New York
MARGE ROUKEMA, New Jersey
BILL LOWERY, California
JAMES K. COYNE, Pennsylvania
DOUGLAS K. BEREUTER, Nebraska
DAVID DREIER, California

Subcommittee on Housing and Community Development

HENRY B. GONZALEZ, Texas, *Chairman*

FERNAND J. ST GERMAIN, Rhode Island
WALTER E. FAUNTROY, District of Columbia
JERRY M. PATTERSON, California
JOHN J. LaFALCE, New York
JAMES J. BLANCHARD, Michigan
DAVID W. EVANS, Indiana
STANLEY N. LUNDINE, New York
MARY ROSE OAKAR, Ohio
BRUCE F. VENTO, Minnesota
ROBERT GARCIA, New York
MIKE LOWRY, Washington
PARREN J. MITCHELL, Maryland
CARROLL HUBBARD, Jr., Kentucky
NORMAN E. D'AMOURS, New Hampshire
CHARLES E. SCHUMER, New York
BARNEY FRANK, Massachusetts
WILLIAM J. COYNE, Pennsylvania
STENY H. HOYER, Maryland

J. WILLIAM STANTON, Ohio
CHALMERS P. WYLIE, Ohio
STEWART B. McKINNEY, Connecticut
THOMAS B. EVANS, Jr., Delaware
JIM LEACH, Iowa
ED BETHUNE, Arkansas
MARGE ROUKEMA, New Jersey
JAMES K. COYNE, Pennsylvania
GEORGE C. WORTLEY, New York
GREGORY W. CARMAN, New York
BILL McCOLLUM, Florida
BILL LOWERY, California
DOUGLAS K. BEREUTER, Nebraska
DAVID DREIER, California

CONTENTS

Page

Hearings held on—
- March 18, 1982 ... 787
- March 23, 1982 ... 1031

Text of H.R. 5568 ... 789

March 18, 1982

Witnesses

Robert R. Masterton, chairman, National Association of Mutual Savings Banks ... 809
Roy G. Green, president, U.S. League of Savings Associations, accompanied by George Briody, president of Fairfield Savings of Chicago, Ill., and Hal Wolfe, president of Capital Savings of Olympia, Wash ... 823
James A. Coles, president of the United Savings of Houston, Tex., and treasurer of the National Savings & Loan League ... 847
William B. Muse, Jr., president of Imperial Savings & Loan Association, Martinsville, Va., representing the American Savings & Loan League, Inc ... 861
Ralph Nader, Public Interest Research Group, accompanied by Jonathan Brown ... 930
Gale Cincotta, chairperson, National People's Action ... 1002
Hal Sisson, legislative representative, Communication Workers of America ... 1013
Martin E. Sloane, executive director, National Committee Against Discrimination in Housing ... 1018

Additional Material Submitted for Inclusion in the Record

Cincotta, Gale, prepared statement ... 1006
Coles, James A., prepared statement on behalf of the National Savings & Loan League ... 850
Correspondence from the minority staff to organizations represented at the hearing, with the responses of the organizations:
- National Association of Mutual Savings Banks ... 880
- National Savings & Loan League ... 870
- U.S. League of Savings Associations ... 887

Green, Roy G.:
- Prepared statement on behalf of the U.S. League of Savings Associations ... 827
- Response to the request of Congressman Schumer for additional information ... 913

Masterton, Robert R., prepared statement on behalf of the National Association of Mutual Savings Banks ... 812
Muse, William B., Jr., prepared statement on behalf of the American Savings & Loan League, Inc ... 864
Nader, Ralph:
- Joint statement on H.R. 5568 by the Public Interest Group, the Communication Workers of America, and the National Committee Against Discrimination in Housing ... 931
- Letter from Jonathan Brown of the Public Interest Group, dated April 20, 1982, responding to the request of Congressman Schumer for additional information ... 969
- Prepared statement with attached brochure regarding the Citizens Utility Board and what to do about rising utility rates ... 943

Sisson, Hal, prepared statement ... 1014

MARCH 23, 1982

WITNESSES

Page
Hon. Richard A. Berman, commissioner of housing and community renewal, New York State, accompanied by Sydelle Knepper, assistant commissioner for development ... 1032
Henry B. Schechter, director, American Federation of Labor and Congress of Industrial Organizations Office of Housing and Monetary Policy ... 1068
Leon N. Weiner, president, National Housing Conference ... 1089
Richard K. Helmbrecht, president, Council of State Housing Agencies, accompanied by Thomas W. White, executive vice president, and Gregg Smith, director, Oregon Housing Division ... 1114
Hon. Bill Emerson, a Representative from the State of Missouri ... 1155
R. Clayton Jones, president, National Association of Housing and Redevelopment Officials ... 1169
John A. McCauley, deputy commissioner, Baltimore Department of Housing and Community Development, spokesman, Council of Large Public Housing Authorities ... 1231
Andrew J. Mooney, executive director, Chicago Housing Authority ... 1265
Roy J. Cleveland, executive director, Navajo Housing Authority, Window Rock, Navajo Nation, Ariz., accompanied by John H. Schuelke, attorney ... 1271
Robert E. Esery, president, National Apartment Association, accompanied by Scott Slesinger, general counsel ... 1299
Ron Shiffman, director, Pratt Institute Center for Community and Environmental Development, Brooklyn, N.Y ... 1316

ADDITIONAL MATERIAL SUBMITTED FOR INCLUSION IN THE RECORD

Berman, Hon. Richard A.:
  Letter, dated March 30, 1982, responding to request of Congressman LaFalce for additional information ... 1059
  Prepared statement ... 1038
Cleveland, Roy J., prepared statement, with attachments, on behalf of the Navajo Housing Authority ... 1275
El Paso Housing Authority, El Paso, Tex., letter dated March 22, 1982, from Salvator F. Canchola, executive director, with attached statement ... 1446
Emerson, Hon. Bill:
  Letter, dated December 7, 1981, from National Association of Home Builders President Herman J. Smith regarding legislation pertaining to the homeownership equity loan program ... 1158
  Text of H.R. 5150 ... 1159
    Factsheet on H.R. 5150 ... 1166
Esrey, Robert E.:
  Letter, dated April 16, 1982, responding to request for additional information from Congressman Schumer ... 1313
  Prepared statement on behalf of the National Apartment Association ... 1303
Frank, Hon. Barney, submission of letter to HUD Secretary Samuel R. Pierce, Jr., dated March 19, 1982, signed by 40 Members of Congress, regarding the future of the section 8 housing program ... 1144
Helmbrecht, Richard K.:
  Prepared statement on behalf of the Council of State Housing Agencies ... 1117
  Response to written question of Congressman St Germain ... 1148
Housing Authority of Gloucester County, Woodbury, N.J., letter dated March 24, 1982, from Frank C. Cossaboon, executive director ... 1451
Jones, R. Clayton:
  NAHRO's comments on the administration's legislative package ... 1211
  NAHRO's policy analysis of the Reagan fiscal year 1983 HUD budget ... 1189
  Prepared statement on behalf of the National Association of Redevelopment Officials ... 1172
  Response to written questions of Chairman Gonzalez ... 1264
  "Summary of CDBG/UDAG Questionnaire Responses" ... 1221
Lowery, Hon. Bill, statement in support of H.R. 5150 ... 1168
McCauley, John A., prepared statement on behalf of the Council of Large Public Housing Authorities ... 1239
Schechter, Henry B.:
  Prepared statement on behalf of the American Federation of Labor and Congress of Industrial Organizations ... 1071

Page

Schechter, Henry B.—Continued
    Response to additional written question of Chairman Gonzalez 1133
Shiffman, Ron:
    Prepared statement 1322
    Studies prepared for the Pratt Institute Center for Community and Environmental Development:
        "Effect of Proposed Changes in Procedures Used To Calculate Tenant Rent Contributions" 1335
        "Impact of a Housing Voucher Program on New York City's Population" 1341
        "Reasons Why Results From the Experimental Housing Allowance Program (EHAP) Should Not Be Relied Upon as Conclusive Support for the Administration's Housing Proposals" 1338
Virgin Islands Housing Authority, Charlotte Amalie, St. Thomas, U.S. Virgin Islands, letter dated March 4, 1982, from Floyd Williams, executive director, with enclosed position paper 1453
Weiner, Leon N., prepared statement, with attachments, on behalf of the National Housing Conference 1096

HOUSING AND URBAN-RURAL RECOVERY ACT OF 1982

THURSDAY, MARCH 18, 1982

House of Representatives,
Committee on Banking, Finance and Urban Affairs,
Subcommittee on Housing and Community Development,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:20 a.m., in room 2128, Rayburn House Office Building, Hon. Henry B. Gonzalez (chairman of the subcommittee) presiding.

Present: Representatives Gonzalez, St Germain, LaFalce, Oakar, Vento, Schumer, Frank, William J. Coyne, Hoyer, Stanton, Thomas B. Evans, Jr., Bethune, Roukema, Wortley, and Carman.

Chairman Gonzalez. The subcommittee will please come to order. Let me explain that the House decided without prior consultation with the subcommittee to open the House session at 10 a.m., and we are going to have a series of votes after a while. But we will find a way to accommodate the witnesses who, in advance we want to thank for their cooperation.

Normally hearings on housing and community development do not require us to bring in witnesses from the mortgage finance community. But we are not operating in normal conditions or in a normal economy.

Where in the past could we look beyond a tight-money period to a healthy resurgence in housing, today we find the savings and loan industry on the verge of collapse—or, to put it in brighter terms, on the edge of a slide into oblivion. The consequence of the disastrous shape of the savings and loan industry is that no one is certain just where the mortgage money of the future is going to come from, or in what form, or at what cost.

For the first time ever, we are operating in a situation in which the long-term outlook for housing is not good. We are not in a money crunch; we are in a situation in which the financial underpinnings of the housing industry are close to shattering.

What we do in this bill, as far as housing stimulus programs go, and other forms of housing assistance are concerned, will help preserve the housing industry, and will help us keep together the skills and spirit of enterprise that are essential if we are going to build the housing that the Nation needs.

But these programs are by their nature only marginal medicine for housing. The kind of housing industry that we have had, and the kind that we must have in the future, must be one that is able to draw its primary energy and resources from private sources of financing. Housing assistance programs can be a catalyst—and that is what they have been. Last year the most significant fact of this economy was that the American economy is inextricably linked with housing construction and construction in general in the economy. These programs have not been and are not intended to be a substitute for the great engine of enterprise—an engine fueled by the savings and loan industry.

The housing business is starving for lack of credit—or put another way, lack of fuel. The source of that fuel, the thrift industry, is in terribly bad health.

If we want to preserve the housing industry in the successful form that it has operated in, we have to preserve its financing source—the thrift industry.

It is for that reason that we are including in these hearings a panel of witnesses from the savings and loan industry. We need to discover what can be done to hold together not just the builders, but those who provide the credit that fuels their business.

If we fail in this effort, this parallel effort to save builders and their financiers, alike, we will have only two choices left open. First, we can suffer housing shortages and excessive housing costs, and we can return to the days when a third of the Nation was ill-housed—a choice that I do not think is acceptable to the Nation. Second, we can substitute Government financing for the private financing that has been the primary source of housing credit for these last five decades. I do not think many of my colleagues would relish that prospect, nor that many would recommend it. But the truth is that unless we have a recognition of the impact of continuing along present lines, that is what will be left to us.

This is a crucial year for housing—maybe the most critical year of all time, and that is why we have to consider what our witnesses this morning have to say about the health of housing finance, and what they recommend as a way to keep their business alive, and housing available for our citizens.

At this point, I would recognize the distinguished minority leader of the subcommittee, Mr. Stanton.

Mr. STANTON. Thank you, very much, Mr. Chairman.

Ladies and gentlemen, today the Housing Subcommittee begins several days of hearings on H.R. 5568, the Home Mortgage Capital Stabilization Act as introduced by our chairman.

Although this bill normally should have been referred to the Financial Institutions Supervision, Regulation, and Insurance Subcommittee, I can appreciate the chairman's desire to move this legislation quickly by considering it as part of the annual housing authorization.

[The text of H.R. 5568 follows:]

I

97TH CONGRESS
2D SESSION

H. R. 5568

To revitalize the housing industry by strengthening the financial stability of home mortgage lending institutions and ensuring the availability of home mortgage loans at reasonable rates.

IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 23, 1982

Mr. ST GERMAIN introduced the following bill; which was referred to the Committee on Banking, Finance and Urban Affairs

---

A BILL

To revitalize the housing industry by strengthening the financial stability of home mortgage lending institutions and ensuring the availability of home mortgage loans at reasonable rates.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SHORT TITLE

SECTION 1. This Act may be cited as the "Home Mortgage Capital Stability Act".

CAPITAL PARTICIPATION NOTES AND EARNINGS STABILIZATION PAYMENTS

SEC. 2. (a) Section 13 of the Federal Deposit Insurance Act (12 U.S.C. 1823) is amended by adding at the end thereof of the following:

"(h)(1) The Corporation may provide assistance under this subsection to any insured bank which the Corporation determines under paragraph (2) to be eligible for such assistance.

"(2) No assistance may be provided under this subsection unless the Corporation determines that—

"(A) the net worth of the insured bank involved is less than 2 per centum of such insured bank's assets;

"(B) such insured bank has sustained losses for any two consecutive quarters which occur during any period beginning with the two quarters which are the most recently completed quarters prior to the effective date of the Home Mortgage Capital Stability Act;

"(C) not less than 20 per centum of such insured bank's loan portfolio consists of mortgages which are secured by property on which there is located a one- to four-family residence or which are secured by individual units in a condominium or cooperative project;

"(D) such insured bank demonstrates a need for such assistance and has reasonable prospects for long-term viability; and

"(E) such insured bank has agreed to comply with all requirements established by the Corporation, including requirements—

"(i) to repay such assistance in accordance with the provisions of this subsection;

"(ii) to provide quarterly reports to the Corporation regarding such insured bank's financial condition and lending practices;

"(iii) that, during the period in which such insured bank owes any amount to the Corporation under this subsection, not less than 50 per centum of its annual net new deposits (as determined by subtracting from the deposits for each year the total amount of withdrawals and of interest and dividends credited during each year) shall be used to issue mortgages which—

"(I) are secured by property on which there is located a one- to four-family residence or are secured by individual units in a condominium or cooperative project;

"(II) are made to first-time home buyers;

"(III) are made at a rate of interest which, on the date of issuance of the mortgage, is not more than 1 per centum greater than the average cost of funds for such insured bank; and

"(IV) are made in an amount which does not exceed the applicable amount specified in section 203(b)(2) of the National Housing Act; and

"(iv) which will permit an insured bank to satisfy up to 50 per centum of the requirement specified in clause (iii) by purchasing securities which are backed by mortgages described in clause (iii) and issued after the date on which such insured bank receives assistance under this subsection for the first time.

"(3)(A) The Corporation may purchase capital participation notes which are issued by any qualified insured bank.

"(B) The amount of capital participation notes purchased by the Corporation from any qualified insured bank shall be equal to the difference between such qualified insured bank's net worth and an amount equal to 2 per centum of such qualified insured bank's assets.

"(C) All amounts received from the sale of capital participation notes shall be used solely to increase the net worth of such qualified insured bank.

"(4)(A) During the two-year period following the date on which the Corporation purchases capital participation notes from a qualified insured bank, the Corporation, on a quarterly basis, may make earnings stabilization payments to such qualified insured bank in an amount equal to the earnings losses incurred by such qualified insured bank during the previous quarter.

"(B) After such two-year period, earnings stabilization payments may be made to such qualified insured bank only if the Corporation certifies that the continued earnings losses involved are caused by general market conditions and not by the actions of such qualified insured bank.

"(5)(A) When the net worth of a qualified insured bank reaches 3 per centum, or upon the expiration of five years after the date on which such qualified insured bank first receives assistance under this subsection, whichever occurs first, such qualified insured bank shall begin to repay to the Corporation the amounts received under this subsection by such qualified insured bank plus interest on such amounts at a rate determined by the Secretary of the Treasury taking into consideration the current average yield on outstanding marketable obligations of the United States of comparable maturities during the month preceding the receipt of the amount involved.

"(B) The total annual repayment to the Corporation shall not be less than 50 per centum of the net income, after taxes, of such qualified insured bank for the year involved.

"(6) During any period in which a qualified insured bank which has a stock form of ownership owes any amount to the Corporation under this subsection, such qualified insured bank may not pay dividends to its shareholders.

"(7) For purposes of this subsection—

"(A) the term 'net worth'—

"(i) with respect to an insured bank which is not a mutual savings bank, shall have the same meaning given the term 'capital' as defined by the appropriate supervisory agency; and

"(ii) with respect to an insured bank which is a mutual savings bank, shall have the same meaning given the term 'surplus' as defined by the Corporation; and

"(B) the term 'qualified insured bank' means an insured bank which the Corporation determines under paragraph (2) to be eligible for assistance under this subsection.".

(b) Section 406 of the National Housing Act (12 U.S.C. 1729) is amended by adding at the end thereof the following:

"(g)(1) The Corporation may provide assistance under this subsection to any insured institution which the Corporation determines under paragraph (2) to be eligible for such assistance.

"(2) No assistance may be provided under this subsection unless the Corporation determines that—

"(A) the net worth of the insured institution involved is less than 2 per centum of such insured institution's assets;

"(B) such insured institution has sustained losses for any two consecutive quarters which occur during any period beginning with the two quarters which are the most recently completed quarters prior to the effective date of the Home Mortgage Capital Stability Act;

"(C) not less than 20 per centum of such insured institution's loan portfolio consists of mortgages which are secured by property on which there is located a one- to four-family residence or which are secured by individual units in a condominium or cooperative project;

"(D) such insured institution demonstrates a need for such assistance and has reasonable prospects for long-term viability; and

"(E) such insured institution has agreed to comply with all requirements established by the Corporation, including requirements—

"(i) to repay such assistance in accordance with the provisions of this subsection;

"(ii) to provide quarterly reports to the Corporation regarding such insured institution's financial condition and lending practices;

"(iii) that, during the period in which such insured institution owes any amount to the Corporation under this subsection, not less than 50 per centum of its annual net new deposits (as determined by subtracting from the deposits for each year the total amount of withdrawals and of interest and dividends credited during each year) shall be used to issue mortgages which—

"(I) are secured by property on which there is located a one- to four-family residence or are secured by individual units in a condominium or cooperative project;

"(II) are made to first-time home buyers;

"(III) are made at a rate of interest which, on the date of issuance of the mortgage, is not more than 1 per centum greater than the average cost of funds for such insured institution; and

"(IV) are made in an amount which does not exceed the applicable amount specified in section 203(b)(2) of the National Housing Act; and

"(iv) which will permit an insured institution to satisfy up to 50 per centum of the requirement specified in clause (iii) by purchasing securities which are backed by mortgages described in clause (iii) and issued after the date on which such insured institution receives assistance under this subsection for the first time.

"(3)(A) The Corporation may purchase capital participation notes which are issued by any qualified insured institution.

"(B) The amount of capital participation notes purchased by the Corporation from any qualified insured institution shall be equal to the difference between such qualified insured institution's net worth and an amount equal to 2 per centum of such qualified insured institution's assets.

"(C) All amounts received from the sale of capital participation notes shall be used solely to increase the net worth of such qualified insured institution.

"(4)(A) During the two-year period following the date on which the Corporation purchases capital participation notes from a qualified insured institution, the Corporation, on a quarterly basis, may make earnings stabilization payments to such qualified insured institution in an amount equal to the earnings losses incurred by such qualified insured institution during the previous quarter.

"(B) After such two-year period, earnings stabilization payments may be made to such qualified insured institution only if the Corporation certifies that the continued earnings losses involved are caused by general market conditions and not by the actions of such qualified insured institution.

"(5)(A) When the net worth of a qualified insured institution reaches 3 per centum, or upon the expiration of five years after the date on which such qualified insured institution first receives assistance under this subsection, whichever occurs first, such qualified insured institution shall begin to repay to the Corporation the amounts received under this subsection by such qualified insured institution plus interest on such amounts at a rate determined by the Secretary of the Treasury taking into consideration the current average yield on outstanding marketable obligations of the United States of comparable maturities during the month preceding the receipt of the amount involved.

"(B) The total annual repayment to the Corporation shall not be less than 50 per centum of the net income, after taxes, of such qualified insured institution for the year involved.

"(6) During any period in which a qualified insured institution which has a stock form of ownership owes any amount to the Corporation under this subsection, such qualified insured institution may not pay dividends to its shareholders.

"(7) For purposes of this subsection—

"(A) the term 'net worth' shall have the same meaning given the term 'reserves' as defined in section 403(b) of the National Housing Act and in the regulations issued pursuant to such section; and

"(B) the term 'qualified insured institution' means an insured institution which the Corporation determines under paragraph (2) to be eligible for assistance under this subsection.".

"(c) Section 208 of the Federal Credit Union Act (12 U.S.C. 1788) is amended by adding at the end thereof the following:

"(e)(1) The Board may provide assistance under this subsection to any insured credit union which the Board determines under paragraph (2) to be eligible for such assistance.

"(2) No assistance may be provided under this subsection unless the Board determines that—

"(A) the net worth of the insured credit union involved is less than 2 per centum of such insured credit union's assets;

"(B) such insured credit union has sustained losses for any two consecutive quarters which occur during any period beginning with the two quarters which are the most recently completed quarters prior to the effective date of the Home Mortgage Capital Stability Act;

"(C) not less than 20 per centum of such insured credit union's loan portfolio consists of mortgages which are secured by property on which there is located a one- to four-family residence or which are secured by individual units in a condominium or cooperative project;

"(D) such insured credit union demonstrates a need for such assistance and has reasonable prospects for long-term viability; and

"(E) such insured credit union has agreed to comply with all requirements established by the Board, including requirements—

"(i) to repay such assistance in accordance with the provisions of this subsection;

"(ii) to provide quarterly reports to the Board regarding such insured credit union's financial condition and lending practices;

"(iii) that, during the period in which such insured credit union owes any amount to the Board under this subsection, not less than 50 per centum of its annual net new deposits (as determined by subtracting from the deposits for each year the total amount of withdrawals and of interest and dividends credited during each year) shall be used to issue mortgages which—

"(I) are secured by property on which there is located a one- to four-family residence or are secured by individual units in a condominium or cooperative project;

"(II) are made to first-time home buyers;

"(III) are made at a rate of interest which, on the date of issuance of the mortgage, is not more than 1 per centum greater than the average cost of funds for such insured credit union; and

"(IV) are made in an amount which does not exceed the applicable amount specified in section 203(b)(2) of the National Housing Act; and

"(iv) which will permit an insured credit union to satisfy up to 50 per centum of the requirement specified in clause (iii) by purchasing securities which are backed by mortgages described in clause (iii) and issued after the date on which such insured credit union receives assistance under this subsection for the first time.

"(3)(A) The Board may purchase capital participation notes which are issued by any qualified insured credit union.

"(B) The amount of capital participation notes purchased by the Board from any qualified insured credit union shall be equal to the difference between such qualified insured credit union's net worth and an amount equal to 2 per centum of such qualified insured credit union's assets.

"(C) All amounts received from the sale of capital participation notes shall be used solely to increase the net worth of such qualified insured credit union.

"(4)(A) During the two-year period following the date on which the Board purchases capital participation notes from a qualified insured credit union, the Board, on a quarterly basis, may make earnings stabilization payments to such qualified insured credit union in an amount equal to the earnings losses incurred by such qualified insured credit union during the previous quarter.

"(B) After such two-year period, earnings stabilization payments may be made to such qualified insured credit union only if the Board certifies that the continued earnings losses involved are caused by general market conditions and not by the actions of such qualified insured credit union.

"(5)(A) When the net worth of a qualified insured credit union reaches 3 per centum, or upon the expiration of five years after the date on which such qualified insured credit union first receives assistance under this subsection, whichever occurs first, such qualified insured credit union shall begin to repay to the Board the amounts received under this subsection by such qualified insured credit union plus interest on such amounts at a rate determined by the Secretary of the Treasury taking into consideration the current average yield on outstanding marketable obligations of the United States of comparable maturities during the month preceding the receipt of the amount involved.

"(B) The total annual repayment to the Board shall not be less than 50 per centum of the net income, after taxes, of such qualified insured credit union for the year involved.

"(6) For purposes of this subsection—

"(A) the term 'net worth' shall have the same meaning given the term 'reserves' as defined in section

116 of this Act and the regulations issued pursuant to such section; and

"(B) the term 'qualified insured credit union' means an insured credit union which the Board determines under paragraph (2) to be eligible for assistance under this subsection.".

HOME MORTGAGE CAPITAL STABILITY FUND

SEC. 3. (a)(1) There is hereby established in the Treasury of the United States a Home Mortgage Capital Stability Fund (hereinafter in this Act referred to as the 'Fund') which shall be used as a revolving fund by—

(A) the Federal Deposit Insurance Corporation to carry out the provisions of section 13(h) of the Federal Deposit Insurance Act;

(B) the Federal Home Loan Bank Board to carry out the provisions of section 406(g) of the National Housing Act; and

(C) the National Credit Union Administration to carry out the provisions of section 208(e) of the Federal Credit Union Act.

(2) All repayments of assistance made under such sections shall be deposited in the Fund.

(b) There are hereby authorized to be appropriated without fiscal year limitation $7,500,000,000 to carry out the functions of the Fund. Such funds shall remain available until expended.

REPORTS TO CONGRESS

SEC. 4. The Federal Home Loan Bank Board, the Board of Directors of the Federal Deposit Insurance Corporation, and the National Credit Union Administration Board shall each transmit a quarterly report to each House of the Congress specifying the types and amounts of assistance provided to each depository institution under the amendments made by section 2 of this Act.

EFFECTIVE DATE

SEC. 5. This Act shall take effect on the date of the enactment of this Act.

Mr. **Stanton**. At the outset, we should acknowledge the vital and historic role that financial institutions in particular have played in the housing industry in fostering the dream of American homeownership. The witnesses this morning personify that important role. Their testimony accurately describes the problems that are real and in large measure are the results of double-digit inflation: high-interest rates, and counterproductive, though well-intentioned, regulation.

This legislation and other alternatives that will arise during these hearings, are designed to assist the troubled housing and thrift institutions in this country. I congratulate the chairman for presenting us with an imaginative proposal. I congratulate him further for meeting and facing the problem. However, we must recognize from the start that the problems of the thrift institutions will not be solved by bailing out failing institutions with *x* billions of dollars. And in the chairman's bill, it is commendable that 50 percent of the net new deposits should go for mortgages for first time home buyers, but how can thrifts attract new deposits if they lack the competitive services demanded by their customers?

Likewise, it is admirable that assisted institutions be required to lend any new funds at only 1 percent above their average cost of funds. Yet, if these funds are to be repaid, based upon the Treasury's borrowing rate, I wonder if the negative earnings spread which many of these institutions face would only be perpetuated. This approach could help some institutions temporarily, but it does nothing to correct the structural and more fundamental problems which exist today.

A more proper solution necessarily must be a comprehensive one, a solution that offers not only immediate help to those institutions that want to compete in the future, but also the powers and the foundation to do so.

We must begin to modernize the 50-year old banking statutes which are too often worshipped as sacrosanct and inviolate. In this context, a recent New York Times editorial on financial reform offered three axioms which this committee should keep in mind.

They are: First, when in doubt, choose competition; second, hold subsidies to a minimum; and third, give preference to Federal rules.

Mr. Chairman, I join you in these hearings, and I welcome, as I stated before, your intentions in meeting this problem. I also acknowledge the recent joint letter from the trade groups, two of which are represented here today, and I concur in their sentiment that we should work out a solution that affirms the fact that Congress stands behind the integrity of insured institutions in federally chartered depository institutions.

In the next few minutes we are about to vote on a resolution, a concurrent resolution with the other body, reassuring that federally chartered deposit institutions and other insitutions that are insured to the amount of $100,000 for individuals are indeed backed by the full faith and credit of the Federal Government.

In the same spirit of cooperation as we met on this resolution, Mr. Chairman, I look forward to working with you and my other colleagues to find a solution to the problems of the housing and thrift institutions, and I thank you very much, Mr. Chairman.

Chairman **Gonzalez**. Thank you, Mr. Stanton. We would again, recognize the chairman of the full committee, who is also the ranking member of the subcommittee, and it is a pleasure to recognize him at this point, Mr. St Germain.

Mr. **St Germain**. Thank you, Mr. Chairman. This session marks the opening, as has been stated, in our hearings on H.R. 5568, the Home Mortgage Capital Stability Act.

This legislation deals with the critical problems facing the housing and mortgage lending industries. It is designed to provide short-term relief for mortgage lending institutions facing temporary earnings losses in the current high-interest market.

To qualify for assistance lenders must show specific need for help, a record of mortgage lending, and a willingness to remain in the home mortgage lending field.

The supporters of H.R. 5568 believe that it is in the national interest to preserve a mortgage lending industry and that is essential to the economic well-being of this Nation that the housing industry be revitalized and a source of funds maintained for home buyers.

I am aware that the well publicized plight of the thrift industry has brought forth a multitude of suggested solutions. At some point, this "Solution of the Week" game show must end and we must deal forthrightly with the problem.

I sincerely hope that the serious problems of this industry do not become a partisan issue in this election year. I hope that the reluctance of some to help push this legislation is not because they are willing to let these critical issues slide while waiting for a task force or some miracle cure that can provide their administration with the credit for the headlines.

Let us get on with the job and forget the politics. Surely, we owe that much to the American people on an issue that so vitally affects the entire Nation.

My original bill provided that loans for capital infusion be in the form of cash drawn from a special fund with the Treasury Department. I have been looking at the issue closely, trying to devise a means of reducing any budget impact. I now plan to amend the H.R. 5568 and substitute "net worth guarantees" in place of the outlay of Treasury funds. Under this plan, guarantees would be issued to troubled institutions in amounts sufficient to return their net worth to at least 2 percent. The guarantees would count as part of the institution's net worth, but they would not be cashed—and the money drawn from Treasury—unless the institution actually went down.

I am convinced that very few institutions will fail—if this guarantee program is enacted in a timely fashion—and as a result there will be only a minimal impact on the budget. In fact, if the administration's economic experts are correct, the economy will right itself soon, interest rates will be coming down, and, under this scenario, the cost of the program will be zero.

I am not counting on the administration's experts being right for the first time, but this program is sufficient to tide the mortgage lending industry over the rocky road that we are now on.

All of us, I am sure, wish current economic conditions did not require assistance legislation. But, it would be irresponsible for the committee to dodge the issue, to ignore the problems and fail to take action, charges about "bailouts" notwithstanding. We must have the political courage to do the right thing.

I would state further, that there is no doubt that this is not the long-term solution to the problems of the thrift industry. However, my feeling about this legislation is quite similar to the way I felt about the regulators bill. There are two items that have to be addressed. This bill deals with a situation that has to be addressed immediately. Added powers and changes in structure have to be addressed as well.

The latter will not help the situation that prevails in the marketplace today; and certainly, it should become apparent that the adoption and the enactment of a restructuring bill, is not going to be as easy as some had thought. We found that out when we addressed the regulators bill, here in the committee, in the Rules Committee, and on the floor.

On the Senate side, our counterparts have found as well that there is much controversy over that legislation. It is not going to be enacted overnight. It will be, I have no doubt of the fact. Working in conjunction with our esteemed ranking minority member, we are going to get something done, but it is going to be difficult.

I, too, want to note the fact that in this spirit of bipartisan cooperation, we have a resolution on the floor at this very moment; we will be voting on it in the next 15 minutes. It will reassure the American people, as Bill Stanton said, that the full faith and credit of the U.S. Government behind insured deposits up to $100,000.

This is another step that is vital and necessary given some of the irresponsible statements that have been made over the past few months.

I thank the chairman for this time. I assume that we are going over to vote, and that now that you have heard our testimony, we will listen to your testimony when we return.

Chairman Gonzalez. In view of the fact that we do have an aye-and-nay vote pending, we have less than 10 minutes. In order to afford every member a chance to be present and recording his vote, on this successive series of six votes, we will have 5 minutes apart. The subcommittee will stand recessed until about 11:00 a.m, sharp.

[Recess.]

Chairman Gonzalez. The subcommittee will proceed with the hearing. And we apologize for the delay and the interruption.

We were going to recognize Mr. Masterton first. But, let me announce for the sake of the record that we have on this panel this morning, Mr. Robert Masterton, chairman of the National Association of Mutual Savings Banks; Mr. Roy G. Green, president of the U.S. League of Savings Associations; and Mr. James Coles, who is the president of the United Savings Association of Texas, representing the National Savings and Loan League.

We welcome this fellow Texan, and Mr. William B. Muse, Jr., president of the Imperial Savings and Loan Association, Martinsville, Va., representing the American Savings Loan League.

Mr. Masterton?

STATEMENT OF ROBERT R. MASTERTON, CHAIRMAN, NATIONAL ASSOCIATION OF MUTUAL SAVINGS BANKS

Mr. **MASTERTON**. Thank you, Mr. Chairman. My name is Robert R. Masterton and I am chairman of the National Association of Mutual Savings Banks, and president of the Maine Savings Bank in Portland, Maine.

I will be delivering an abbreviated version of our testimony, our full testimony is on file.

Chairman **GONZALEZ**. If there is no objection, what we can do is offer for the record at this point your prepared text, which you submitted. We want to thank you for having submitted it in advance, giving us a chance to examine it and then you may proceed as you see fit, summarizing or otherwise.

Mr. **MASTERTON**. Thank you Mr. Chairman, we very much appreciate the opportunity to present the views of the savings bank industry on H.R. 5568.

The National Association of Mutual Savings Banks heartily applauds the development of this creative proposal for dealing with the rapidly deteriorating condition of the Nation's thrift and housing industries. May I also add, that we strongly support the thrust and purpose of this legislation, and we commend Chairman St Germain and his colleagues for taking the initiative and innovative steps in addressing an increasingly critical problem.

It is hardly a secret that the Nation's thrift industry faces an imminent crisis in the current high interest rate environment. Thrift institutions are in trouble because they did what Government required or encouraged them to do. That is make long-term mortgage loans at affordable interest rates to home buyers. At the same time, they have been forced to compete for savings at sharply increased deposit interest rates. As a result, thrift institutions are suffering large scale deposit outflows, massive operating losses and rapidly shrinking net worth positions.

The plight of the housing industry is equally well known. Prolonged high interest rates and the inability of thrift institutions to generate mortgage credit have had a shattering effect on the housing sector.

In our judgment, present regulatory policies are not an adequate response to the thrift problem. As a result of present policies, there will be a continuous waive of supervisory mergers, involving literally hundreds of thrift institutions in the months ahead. Accompanied by uninterrupted adverse publicity, this process threatens to undermine confidence in the soundness of the entire financal system.

Ultimately the present regulatory posture points to the subsidized consolidation of a huge number of independent community oriented thrift institutions into a relatively small number of nationwide depository organizations. Thus, our Nation faces a radical revamping of the financial structure by regulatory fiat, without adequate congressional consideration of the public's interest in the outcome.

Action by the Congress is vitally needed, therefore, to maintain confidence in the financial system, to preserve the structure of community-oriented thrift institutions, and to revive the beleaguered housing industry.

With respect to the cost of the assistance programs, we take a back seat to no one in our support for forceful action to reduce massive budgetary deficits. It must be recognized, however, that the Federal Government's commitment to protect the safety of depositor's funds was established many years ago, by the adoption of Federal Deposit Insurance. As a result, the Federal Government has an enormous contingent liability, which will inevitably be translated into increased budgetary expentidures in the present difficult environment.

Failure to take any action in the present crisis will result in a drain on the budget. And may be far more costly in the long run than a soundly conceived program of direct assistance.

H.R. 5568 recognizes that something needs to be done quickly, to assist thrift institutions and housing. This legislation would provide for cash infusions to qualify depository institutions to restore and maintain their net worth at 2 percent of assets. More recently, and again, today, Chairman St Germain, has suggested a possible modification under which institutions would be provided a net worth guarantee rather than cash.

One of our main concerns relates to the need for strengthening earnings and the types of assistance that are most appropriate in addressing the interrelated problems of both earnings and net worth. While bolstering capital is the most immediate priority, weak earnings are the root cause of thrift institutions' problems. Unless the earnings problem is addressed soon, increasing numbers of thrift institutions will inevitably deplete net worth positions and require capital assistance.

Net worth could be restored and maintained at the specified levels through the use of Federal Guarantees, but without any immediate Treasury outlays.

Paralleling the net worth guarantee program, which the Congressman and Chairman St Germain have recently outlined, to strengthen earnings, however, will require actual cash outlays. The mechanism could be an exchange of low-rate mortgages for variable rate Federal Agency obligations, indexed to an appropriate Treasury rate. The institution would receive a temporary supplement to its earnings, based on the interest rate spread, between the mortgages and Agency obligations.

The points that we wish to emphasize are: First, that an improvement in earnings is essential to the solution of the thrift institution problem; and second, that cash outlays are needed to improve earnings.

Accordingly, we believe that an effective thrift institution aid package should address both the earnings and the capital problems, utilize Federal guarantees to strengthen capital and reserve cash outlays for improving earnings.

Another major issue, concerning the effectiveness of the housing assistance provision of H.R. 5568, is the following: We fear that these provisions may not provide an adequate stimulus to housing, while placing undue burdens on participating lenders. In this connection, H.R. 5568, would require assisting institutions to allocate

50 percent of net new deposits for home mortgage loans, at rates 1 percentage above their average cost of funds.

From the standpoint of thrift institutions, this requirement has the potential of perpetuating low-yield mortgage holdings, that are at the very heart of their problems. From the standpoint of assisting home buyers, who happen to be in areas with few assisted institutions, they would be effectively barred from taking advantage of such loans. At the same time, institutions with strong net worth positions would not be able to participate in a below market rate program, even though they may be in the best position to do so.

An effective housing program in our judgment, requires wide participation by all types of lenders. The basic objective of the program should be to reduce interest costs to the home buyers, from the present prohibitive levels. The mechanism could be a temporary buy down from current rates with the Federal Government and private lenders sharing the cost of the buy down.

Other aspects of H.R. 5568 also merit careful review. It is important that savings banks and savings and loans associations are treated similarly in terms of being able to utilize capital assistance. As noted in our full statement, this can be accomplished by requiring FDIC and FSLIC to utilize similar standards and by preempting State capital requirements.

As I draw my points to a conclusion, Mr. Chairman, let me tell you, that a soon-to-be released study—to be released, I believe within the next 24 hours—a study conducted by the Wharton Econometric Forecasting Associates, has appraised the relative costs of present regulatory policies as compared with the number of alternative assistance proposals. A major conclusion of this study is that under various scenarios for the U.S. economy, forced mergers of troubled thrift institutions will be far and away more expensive than the alternative assistance proposals contain.

The question then is not whether Federal funds will be spent in addressing the thrift industry problem Federal funds will have to be spent in any event. The real issue concerns the adequacy of the Federal Government's response to the current crisis, as well as the future structure of the financial system, when it emerges from the current crisis.

A soundly constructed assistance package will enable individual thrift institutions to survive until their earnings are strengthened through the rollover of their low-yield mortgages, and Federal economic policy succeeds in bringing interest rates down.

Such an assistance package will stimulate the depressed housing industry and thereby hasten recovery of the overall economy, and strengthen the Federal tax revenues. It will provide an opportunity for thoughtful consideration of the future financial structure, by the Congress, where the fundamental responsibility lies.

Above all, the adoption of an assistance package will help preserve the public's confidence in the financial system.

In conclusion, Mr. Chairman, H.R. 5568, represents a crucially important first step in developing a program to provide assistance to thrift institutions and to the housing industry. Our comments are offered as a contribution to what promises to be a constructive dialog. We welcome the opportunity to work with the committee in any further development of this vitally needed program.

Thank you.

[Mr. Masterton's prepared statement, on behalf of the National Association of Mutual Savings Banks, follows:]

Statement
of the
National Association of Mutual Savings Banks
on
H.R. 5568, The Home Mortgage Capital Stability Act
Before the
Subcommittee on Housing and Community Development
of the
Committee on Banking, Finance and Urban Affairs
U. S. House of Representatives
March 18, 1982

Mr. Chairman, my name is Robert R. Masterton. I am Chairman of the National Association of Mutual Savings Banks, and President of the Maine Savings Bank in Portland, Maine. The National Association represents the nation's 437 savings banks. Located in 16 states, savings banks are basically community-oriented financial institutions. In the areas where they are most heavily concentrated, savings banks are the largest holders of consumer savings as well as the dominant mortgage lenders among the various types of depository institutions. Our industry's assets total $176 billion.

I appreciate the opportunity to present the views of the savings bank industry on H.R. 5568, the Home Mortgage Capital Stability Act, and on the issues raised by that legislation.

Summary of Savings Bank Industry Position on H.R. 5568

Mr. Chairman, the National Association heartily applauds the development of this creative proposal for dealing with the rapidly deteriorating condition of the nation's thrift and housing industries. For many months, we have urged that a comprehensive federal program is vitally needed to address the thrift institution problem. Until recently, however, we have been frustrated by the apparent lack of concern in Washington about a developing financial crisis. We have been equally frustrated by the Administration's apparent willingness to depend on present regulatory mechanisms to handle the job.

In our judgment, present regulatory policies are not an adequate response. They rely almost solely on supervisory mergers. As a result, there will be a continuous wave of such mergers, involving literally hundreds of thrift institutions in the months ahead. Accompanied by uninterrupted adverse publicity, this process threatens to undermine confidence in the soundness of the entire financial system. Present policies, furthermore, will do nothing to alleviate depressed conditions in the housing and related industries.

Ultimately, the present regulatory posture points to the subsidized consolidation of a huge number of independent, community-oriented thrift institutions into a relatively small number of nationwide depository organizations. Thus, our nation faces a radical revamping of the financial structure by regulatory fiat, without adequate Congressional consideration of the public's interest in the outcome.

Action by the Congress is needed, therefore, to maintain confidence in the financial system, to preserve the structure of community-oriented thrift institutions and to revive the beleaguered housing industry. H.R. 5568 recognizes that something needs to be done quickly to assist thrift institutions and housing in these critical times. It will send a clear signal to the public that the government will stand behind the nation's thrift system. It will provide an indispensable first step toward recovery.

Our statement will discuss in detail some of the major issues raised by this proposal. At this point, I wish to reiterate that the National Association strongly supports the thrust and purpose of H.R. 5568. This legislation has initiated what we all hope will be a fruitful dialogue and prompt action on solutions to the critical problems confronting the thrift and housing industries.

Budgetary Impact of Proposed Assistance Programs

At the outset, it is appropriate to address the budgetary impact of any proposal for aiding the thrift and housing industries. In this regard, we take a back seat to no one in our support for forceful action to reduce massive budgetary deficits and thereby relieve inflationary and interest rates pressures. For many years, we have been strongly urging that deficits be reduced. This remains an urgent national priority.

There is no inconsistency between efforts to reduce the federal deficit and efforts to develop a well-structured assistance package for the thrift industry. The federal government's commitment to protect the safety of depositors' funds was established 50 years ago by the adoption of federal deposit insurance. As a result, the federal government has an enormous contingent liability, which will inevitably be translated into increased budgetary expenditures in the present difficult environment. In this regard, the seven assisted savings bank mergers to date have involved assistance of over $1 billion, and this is only the tip of the iceberg.

Failure to take any action in the present crisis will itself result in a drain on the budget, and may be far more costly in the long-run than a soundly conceived program of direct assistance. The cost of pursuing present policies will be reflected in mounting subsidies for mergers of troubled institutions, particularly as merger partners become more difficult to find. It will be reflected, as well, in the lost tax revenue resulting from the continued devastation of the housing and related industries.

The situation was properly described in an editorial in the February 26 Washington Post:

> "The crucial decision to provide subsidies was taken a long time ago...when the federal government began providing deposit insurance. The only question now is the form of subsidy -- and whether it will be the large amounts that immediate aid will require, or the much larger ones required later to pay off depositors after failure, when the losses will have continued longer."

In this regard, a soon-to-be-released study conducted by Wharton Econometric Forecasting Associates has appraised the relative cost of present regulatory policies as compared with a number of alternative assistance proposals. A major conclusion of this study is that under various scenarios for the U. S. economy, forced mergers of troubled thrift institutions will be, far and away, more expensive than the alternative assistance proposals.

The question, then, is not whether federal funds will be spent in addressing the thrift industry problem. Federal funds will have to be spent in any event. The real issues concern the adequacy of the federal government's response to the current crisis, as well as the future structure of the financial system when it emerges from the current crisis.

A soundly-constructed assistance package will enable individual thrift institutions to survive until their earnings are strenthened through the rollover of their low-yield mortgages, and federal economic policy succeeds in bringing interest rates down. Such an assistance package will stimulate the depressed housing industry, and thereby hasten recovery of the overall economy and strengthen federal tax revenues. It will provide an opportunity for thoughtful consideration of the future financial structure by the Congress, where the fundamental responsibility lies. Above all, prompt adoption of an assistance package will help preserve the public's confidence in the financial system.

Condition of the Thrift and Housing Industries

By now, it is hardly a secret that the nation's thrift industry faces an imminent crisis in the current high interest rate environment. Savings banks and savings and loan associations are caught in a squeeze between soaring deposit interest costs and lagging earnings on their large holdings of low-yield, long-term, fixed-rate mortgage loans.

Essentially, thrift institutions are in trouble because they did what government required or encouraged them to do -- make long-term mortgage loans at affordable interest rates to home buyers. At the same time, they have been forced to compete for savings at sharply increased deposit interest rates, because of the failure of federal anti-inflationary policy, and because of premature deregulation actions by the Depository Institutions Deregulation Committee. As a result, thrift institutions are suffering large-scale deposit outflows, massive operating losses and rapidly shrinking net worth positions.

Last year, savings banks suffered an all-time record deposit loss of $14 billion, excluding interest. Reflecting this deposit drain, as well as the inability of home buyers to pay stratospheric mortgage interest rates, net growth in holdings of mortgage loans and mortgage-backed securities was essentially zero for the industry as a whole.

On the bottom-line, savings banks in 1981 sustained a loss of $1.5 billion, also far more than in any previous year. As a result, the net worth position of the industry declined from 6.6 per cent of assets at the end of 1980 to 5.7 per cent currently. Net worth positions are still ample on an industrywide basis, but have become extremely thin at a rapidly increasing number of individual institutions.

The plight of the housing industry is equally well known. Prolonged high interest rates and the inability of thrift institutions to generate mortgage credit has severely depressed the housing sector. In 1981, housing starts were only slightly above one million units, the lowest level since 1946. Existing home sales were at the lowest level since 1971. Unemployment in the construction industry has approached 20 per cent. Normally the sector that leads the economy out of recession, housing now exerts a major drag on a variety of other industries -- appliances, furnishings, lumber, and other building products -- and on the economy as a whole.

No immediate improvement is in sight. At savings banks, deposit losses will continue and may worsen as a result of the publicity arising from the large number of impending supervisory mergers of thrift institutions. Further bottom-line losses and net worth reductions are all but inevitable. The only question is how large these losses will be in 1982 and beyond. Under reasonable interest rate assumptions, we project that savings banks representing about one-fourth of the industry's assets will run out of net worth by the end of 1982 or early next year.

Given FDIC practices and legal requirements in some savings bank states, supervisory action will be forthcoming well before net worth is totally depleted. In this regard, FDIC typically steps in when net worth positions of savings banks are above the level that would elicit comparable FSLIC action with respect to savings and loan associations. Indeed, supervisory action may be taken in the case of some savings banks even if the institution's net worth is above the level of 2 per cent of assets specified in H.R. 5568.

A decline in interest rates would obviously alleviate the problems facing the thrift and housing industries. But unless interest rates fall deeper and stay down longer than anyone can reasonably expect, these problems will not be ended. Too much damage has already been done to the thrift industry. Even in an optimistic interest rate scenario, bottom-line losses and capital erosion will continue, although at a slower pace. In the housing industry, the devastation has reached such proportions that there are serious doubts that it can respond quickly even in a reduced interest rate climate.

An assistance program for the thrift and housing industries is vitally needed, and needed now.

Issues Raised by H.R. 5568

To achieve this objective, H.R. 5568 would, in general, provide for cash infusions to qualified depository institutions to restore and maintain their net worth at 2 per cent of assets. The assisted institutions would be required to earmark 50 per cent of their net new deposits for home mortgage lending to first-time home buyers at rates one percentage point above their average cost of funds. These institutions would repay the assistance, including interest, to the extent of at least 50 per cent of net income, when net worth reaches 3 per cent of assets or in 5 years, whichever is sooner.

More recently, Chairman St Germain has suggested a possible modification, under which institutions would be provided a "Net Worth Guarantee," rather than cash, when net worth is below 2 per cent of assets. The "Net Worth Guarantee" would have the full backing of the Federal government.

By focusing on net worth positions of thrift institutions, H.R. 5568 unquestionably addresses the most pressing priority. We have a number of questions, however, related mainly to whether the proposal would achieve its full objectives, and with the most efficient and equitable use of federal resources. We realize that this is a concern shared by all Committee members and we offer our comments with a view toward helping to perfect this legislation.

One issue has already been mentioned -- the fact that savings banks are subject to supervisory action at higher net worth levels than savings and loan associations, even higher than 2 per cent of assets in some cases. Partly because of this, only a handful of savings banks currently have net worth positions below 2 per cent, although the number will increase rapidly in the months ahead. There is the prospect that savings banks will be merged by supervisory action before their net worth reaches the 2 per cent level. Depending on interest rate trends, it is also possible that by the time many savings banks qualify, a large part of the assistance available under H.R. 5568 will have been expended.

This situation can be remedied within the spirit of H.R. 5568 by a number of modifications. Federal preemption of state net worth requirements would eliminate the problem of excessively high requirements that would effectively bar some state-chartered institutions from receiving assistance. In administering the program, moreover, FDIC and FSLIC should be required to utilize parallel standards so that savings banks and savings and loan associations in similar circumstances will be treated similarly. This would be broadly analogous to the establishment of parity between FDIC and FSLIC in providing assistance under the House-passed Regulators Bill (H.R. 4603). Language should also be added to make unmistakably clear that capital certificates issued by assisted institutions will be treated as net worth for accounting purposes. These modifications would be entirely consistent with the basic thrust of H.R. 5568 -- to establish a nationwide minimum net worth position for all qualified depository institutions through federal government assistance.

Beyond these modifications, one of our main concerns relates to the need for strengthening earnings, and to the types of assistance that are most appropriate in addressing the inter-related problems of earnings and net worth.

While bolstering capital is the most immediate priority, weak earnings are the root cause of the thrift institution problem. It bears repeating that major earnings losses will continue at thrift institutions in the foreseeable future, because they have large holdings of low-yield mortgages and must compete for savings in a climate of sharply increased deposit interest rates. And unless the earnings problem is addressed soon, increasing numbers of thrift institutions will inevitably deplete net worth positions and require capital assistance.

The interrelated capital and earnings problems can be addressed in two steps, utilizing federal guarantees for capital assistance and cash outlays for strengthening earnings. Thus, net worth could be restored and maintained at the specified level through the use of federal guarantees, but without any immediate Treasury outlays. This would parallel the "Net Worth Guarantee" program which Chairman St Germain recently outlined.

Using the precedent provided by the Federal Home Loan Bank Board in recent mergers, qualified institutions would be able to issue income capital certificates, which count as net worth, and receive in return a promissory note guaranteed by the federal government. Only in the unlikely event that the institution is liquidated would the federal guarantee be triggered or any outlay by the Treasury be required. The income capital certificates and federally-guaranteed notes would be retired as the institution is restored to profitability.

To ensure that profitability is restored, however, means that the earnings problem must be addressed directly. Unless interest rates fall and remain at reduced levels for a protracted period, this can only be accomplished by actual cash outlays. The mechanism could be an exchange of low-rate mortgages for variable-rate federal agency obligations indexed to an appropriate Treasury rate. The institution would receive a supplement to its earnings based on the interest rate spread between the mortgages and agency obligations. This earnings supplement would be reduced, and would be terminated entirely, as mortgage repayments are used to retire the agency obligations and interest rates decline.

The point we wish to emphasize is that an improvement in earnings is essential to the solution of the thrift institution problem, and that cash outlays are needed to improve earnings. By itself, a capital assistance program merely borrows time, particularly if guarantees are utilized. Earnings assistance, on the other hand, helps return the institution to profitability, ensures that capital infusions are repaid and that "Net Worth Guarantees" are retired without Treasury outlays. Accordingly, we believe that an effective thrift institution aid package should address both the earnings and capital problems, utilize federal guarantees to strengthen capital and reserve cash outlays for improving earnings.

Housing Assistance

Another major issue concerns the effectiveness of the housing assistance provisions of H.R. 5568. We fully agree that new initiatives are needed to make more affordable mortgage credit available to home buyers and thereby assist the shattered housing industry. We strongly urge adoption of an effective program for assisting housing, to accompany a thrift institution aid package structured along the lines discussed earlier in this statement.

We fear, however, that the housing assistance provisions of H.R. 5568 may not provide adequate stimulus to housing, while placing undue burdens on participating lenders. In this connection, H.R. 5568 would require assisted institutions to allocate 50 per cent of net new deposits for home mortgage loans at rates one percentage point above their average cost of funds. From the standpoint of thrift institutions, this requirement has the potential of perpetuating low-yield mortgage holdings that are at the heart of their earnings and net worth problems. Loans made under this requirement would carry rates of return below the cost of new funds attracted by the institution as well as below the rates available on other investments. The chief hope for thrift institutions is that, in time, they will be able to roll over their mortgage portfolios at market rates. Anything that delays this process should be avoided if possible.

From the standpoint of assisting home buyers, furthermore, the housing investment requirement would have certain unfortunate effects. Low-rate loans would be available only from institutions receiving assistance. As a result, home buyers who happen to be in areas with few assisted institutions would be effectively barred from taking advantage of such loans. At the same time, institutions with strong net worth positions would not be able to participate in this below-market rate program, even though they may be in the best position to do so.

An effective housing program, in our judgment, requires wide participation by all types of lenders. Such widespread participation is essential in view of the enormity of current housing and mortgage market problems. The basic objective of the program should be to reduce interest costs to home buyers from present prohibitive levels. The mechanism could be a temporary "buy down" from current market rates, with the federal government and private lenders sharing the cost of the buy-down.

Other provisions of H.R. 5568 also merit careful review. For example, in order to qualify for assistance, an institution is required to have at least 20 per cent of its assets in one- to four-family mortgages, condominiums and cooperative units. We believe that mortgage-backed securities and multi-family mortgages should also be included in determining an institution's eligibility for assistance. This would recognize the importance of these instruments in many areas of the country, as well as the institution's record in financing housing needs.

Conclusion

Mr. Chairman, H.R. 5568 represents a crucially important first step in developing a program to provide assistance to thrift institutions and the housing industry. Our comments are offered as a contribution to what promises to be a constructive dialogue. We welcome the opportunity to work with the Committee in the further development of this vitally needed program.

Chairman GONZALEZ. Thank you, Mr. Masterton, for a very good report. We next recognize Mr. Roy Green, president of the U.S. League of Savings Associations.

STATEMENT OF ROY G. GREEN, PRESIDENT, U.S. LEAGUE OF SAVINGS ASSOCIATIONS, ACCOMPANIED BY GEORGE BRIODY, PRESIDENT OF FAIRFIELD SAVINGS OF CHICAGO, ILL., AND HAL WOLFE, PRESIDENT OF CAPITAL SAVINGS OF OLYMPIA, WASH.

Mr. GREEN. Thank you, Mr. Chairman. As Mr. Masterton said, I also have a complete statement that I have submitted for the record, sir, and if it meets with your pleasure, I would like to make a few preliminary remarks in regard to an overview of that.

Chairman GONZALEZ. Well, without objections, I will order that.

Mr. GREEN. Thank you, sir. My name is Roy Green, and I am president of Fidelity Federal Savings & Loan Association of Jacksonville, Fla., and appear here today as chairman of the U.S. League of Savings Associations. Joining me, for your questions, are George Briody, president of Fairfield Savings & Loan Association of Norridge, Ill., and Hal Wolfe, president of Capital Savings & Loan Association of Olympia, Wash.

The U.S. League of Savings Associations welcomes this opportunity to testify before you on the issues raised by H.R. 5568, the Home Mortgage Capital Stability Act.

We very much appreciate the comments of the leadership, when the hearings were opened this morning, about the importance of the preservation of the thrift industry, because of the important role that we think that we have played in providing housing for many Americans in the past.

A financial crisis unquestionably grips the thrift institutions of America. The combination of portfolios filled with low-yielding mortgages and more than 2 years of punishingly high open market rates which increasingly determine what we must offer the public to hold and attract its savings, has resulted in negative earnings and seriously depleted capital positions.

Articles and broadcasts are focusing on thrift institution difficulties, thereby threatening liquidity problems, as well.

If I may, Mr. Chairman, I would like to interrupt my statement here to express my gratitude to the leadership and members of the Banking Committee whose actions have led the way to the tremendous concurrent resolution vote this morning.

This made it, of course, very clear to the American people that the full faith and credit of the United States stands behind deposits of federally insured depository institutions. And I say to you, that this is very, very much appreciated on our part.

Last year, the savings and loan business suffered operating losses of more than $5 billion; in January we lost another $900 million. These losses resulted from a mismatch of some 1½ percent between the yield on our mortgage holdings and our cost of funds. Improvement on our portfolio return proceeds at a snail's pace, while savings costs not only climb, but become locked in. Thus, negative earnings are assured for sometime to come—even if market rates should drop significantly, as we all so fervently hope.

The dollar figures only tell part of the story. The number of thrift institutions is shrinking dramatically. In 1981, 320 were merged. At the interest rates prevailing in February, we project that 1,100 institutions will fall below that critical 2-percent net worth level by the end of the year, and if no Government assistance is forthcoming, another 700 will reach that level by the end of the year in 1983.

To liquidate so many institutions is absolutely not the answer. The cost to the Federal Government would be staggering. Instead, to date, the FSLIC has pursued a policy of ad hoc restructuring through arranged mergers. Merging this many institutions might cut costs to $45 billion and if, and this is a very big if, partners can be found to absorb about half of our industry.

Thus, forced mergers are not the answer either. The Washington Post recently summarized well, the policy dilemma in a recent editorial.

And I quote:

> The crucial decision to provide subsidies was taken a long time ago. When the Government began providing deposit insurance. The only question now is the form, and whether it will be the large amounts that immediate aid will require, or the much larger ones required later * * *

As exhibit 4 of my prepared statement shows, the magnitude of our low-yielding mortgage burden is immense: one-third of our assets return less than 9 percent; roughly two-thirds are below 10½ percent; and only one-sixth are more than 12 percent. The portfolio "drag" is particularly severe in the Northeast and Midwest.

The problems of our institutions are immediate and serious. Equally important is the loss to the Nation of the product we deliver, home mortgage loans.

While we read of other intermediaries coming to the rescue, commercial banks, pension funds—it is abundantly clear that they are either unwilling or unable to do so in anything like the volume of loans we provide in a terrible year like 1981.

Savings and loan managers remain committed to doing what they do best, serving the residential mortgage credit needs of their local communities.

Unless the Congress acts soon, many thrift institutions will not survive long enough to continue this mission.

The real issue is whether the Congress, or the regulators acting under duress, will determine the future structure of the Nation's financial system.

Yes, high interest rates are at the heart of our problem, and those of the housing industry, and the general economy, for that matter. But we cannot wait for Wall Street to be convinced of emerging fiscal policy. We need a program immediately. It will be much, much cheaper if rates fall. But the accumulated damage thus far demands assistance mechanisms right now.

Chairman St Germain has taken the lead with H.R. 5568. Our organization, in conjunction with the Savings Banks, has also been working on a program.

Briefly described, our plan has three parts: Portfolio assistance, capital maintenance, and homebuyer assistance—all temporary.

The portfolio assistance plan would permit us to "warehouse" loans yielding less than 9 percent for up to 3 years by exchanging those mortgages for variable-rate notes. The notes would carry an interest supplement equal to half the difference between the face rate on the loan which is warehoused and the 30-month Treasury rate. For example, if an 8-percent mortgage is exchanged and the 30-month rate is 14 percent, the institution would receive 11 percent—the 8 percent plus the supplement of half the difference, or 3 percent. This swap would be reversed at the end of 3 years.

If Treasury rates remain at mid-February levels, we are talking about a cost of $7.5 billion to the Treasury to turn $250 billion in mortgages at eligible institutions into productive assets. This statement, of course, assumes that further acceleration in the cost of funds does not occur through some haphazard decisions over at the depository institutions deregulation committee.

The second portion of our plan is similar to the "net worth guarantee" discussed recently by Chairman St Germain.

If adopted, it would sustain institutions at a positive 1.5 percent net worth level through the issuance of income capital certificates. These ICC's would be exchanged for the promissory notes of an autonomous agency; the notes would carry a guarantee of principal and interest by the U.S. Treasury. On return to a net worth level above 1.5 percent, income brought into net worth would enable an institution to surrender the notes and redeem its ICC's. Note that there is no Federal outlay here. The cost to the Government, if any, would arise only if the assisted institution was liquidated.

We propose a skeleton agency to handle these two plans, the portfolio assistance and the capital maintenance. The primary orientation of existing supervisory agencies is to protect depositors, not sustain institutions. If necessary, existing agency officials could be installed as the board members of the skeleton agency to maintain continuity with current supervisory activities.

Our final recommendation is for short-term assistance to home buyers. This program would provide an immediate stimulus to the housing market through an interest-rate buydown. We propose that the Treasury and home lending institutions contribute to the buydown. Using our suggested standards, the program could stimulate up to $83.5 billion in mortgage lending in the coming year, which would finance about 1.6 million home sales.

We will also be commenting by separate statement on such excellent initiatives as the multifamily proposal developed by Chairman Gonzalez and Congressman Schumer and the emergency aid proposal for homeowners facing foreclosure.

We also have several observations about Chairman St Germain's excellent initiative, the Home Mortgage Capital Stability Act.

We would prefer to see the dollar assistance available to all depositories which share the same low-yielding mortgage portfolio burden.

Maintaining capital adequacy is vital, too. Whatever the agency or agencies chosen to administer a "net worth guarantee" program, we would recommend that they be relieved of such subjective judgments as the determination of "reasonable prospects for long-term viability."

We also question the housing reinvestment formula set forth in H.R. 5568. We do not object to a home lending obligation per se, but the formula linking the availability of below-market mortgages to recipients of earnings and capital assistance seems unduly restrictive.

In addition, the obligation to issue loans at 1 percent above the average cost of funds would hinder the ability of assisted institutions to rebuild their earnings and capital positions.

Overall, we cannot compliment too much Chairman St Germain's initiative with his legislation to halt the shrinkage of our thrift industry and to provide the support needed to begin a housing recovery.

We just would like, finally, to make the point, that we urgently and desperately need your help, and need it now.

I have appreciated this opportunity to present the view of the U.S. League of Savings Associations and, with my colleagues, look forward to your questions.

Thank you, sir.

[The prepared statement of Mr. Green, on behalf of the U.S. League of Savings Associations, follows:]

Statement of Roy G. Green
Chairman, U.S. League of Savings Associations
To the Subcommittee on Housing and Community Development
Committee on Banking, Finance and Urban Affairs
U.S. House of Representatives

March 18, 1982

MR. CHAIRMAN:

My name is Roy Green. I am President of Fidelity Federal Savings and Loan Association of Jacksonville, Florida and appear today in my capacity as Chairman of the U.S. League of Savings Associations*. Accompanying me are George Briody, President of Fairfield Savings and Loan Association of Chicago, Illinois, and H. T. Wolfe, President of Capital Savings and Loan Association of Olympia, Washington.

The U.S. League welcomes this opportunity to testify on H.R. 5568, "The Home Mortgage Capital Stability Act." We applaud Chairman St Germain and the many Members of the Banking Committee who have introduced this important bill. Their recognition of the need for prompt Congressional action to preserve the housing delivery system of our country is deeply appreciated.

---

*The U.S. League of Savings Associations has a membership of 4,100 savings and loan associations representing over 99% of the assets of the $650 billion savings and loan business. League membership includes all types of associations -- Federal and state-chartered, stock and mutual. The principal officers are: Roy Green, Chairman, Jacksonville, FL; Leonard Shane, Vice Chairman, Huntington Beach, CA; Stuart Davis, Legislative Chairman, Beverly Hills, CA; William B. O'Connell, President, Chicago, IL; Arthur Edgeworth, Director, Washington Operations; Glen Troop, Legislative Director; and Phil Gasteyer, Associate Director, Washington Operations. League headquarters are at 111 East Wacker Drive, Chicago, IL 60601. The Washington Office is located at 1709 New York Avenue, N.W., Wash., D.C. 20006. Telephone: (202)637-8900.

A financial crisis grips the thrift institutions of America. The combination of asset portfolios filled with low-yielding long-term mortgage loans, rapid deregulation of savings to market rate and beyond, and more than two years of punishing open market rate levels has resulted in negative earnings and seriously depleted capital positions. Public anxiety precipitated by articles and broadcasts focusing on thrift difficulties threatens liquidity problems as well.

Last year a net $25 billion (withdrawals less new deposits) flowed out of savings and loan associations. The deposits outflow continued in January, traditionally the strongest month for new deposits. (By contrast, our commercial bank competitors have been enjoying record retail savings activity, see Exhibit 1.)

Last year, the savings and loan business suffered operating losses of more than $5 billion; in January 1982, another $900 million. (As a result, net worth of the industry nationwide has shrunk from $33 billion at the end of 1980 to roughly $27 billion.) These losses are the consequence of the mismatch between the yield on mortgage holdings (9.88% in the second half, 1981) and the cost of funds (11.32%). (Again, for comparison, see the strong positive commercial bank earnings performance, in Exhibit 2, which illustrates the responsiveness of short-term bank assets in this high-rate economic environment.)

With lending activity at a virtual standstill, improvement in the return on our mortgage portfolio proceeds at a snail's pace, while costs continue to climb and become "locked in," particularly with our market-rate, 30-month Small Savers Certificate (which now comprises more than 20% of our savings base). Thus, negative earnings are assured for some period to come -- even if market rates should decline significantly in the near future, as we all so fervently hope.

The dollar figures -- representing, as they do, national averages -- tell only part of the story. The number of thrift institutions is shrinking dramatically. In 1981, 320 savings and loan associations merged; 30% of these mergers were "supervisory" in nature, with 10% requiring assistance from the Federal Savings and Loan Insurance Corporation. Last year's merger activity was more than 2-1/2 times the previous record annual rate and it severely taxed the ingenuity of the FSLIC.

Our projections, as shown in Exhibit 3, indicate that at the interest rate levels prevailing in February, roughly one-third of the nation's savings and loan business (1,100 institutions with $220 billion in assets) will fall below the critical 2% net worth-to-assets level before the end of this year. (The statutory insurance reserve is 3%; intense supervisory concern is expected at 2% net worth ratios.) Without Government assistance, another 700 institutions with $140 billion in assets -- will reach this point in 1983 if such rate levels persist.

To liquidate so many institutions, with assets of that magnitude ($360 billion), would cost the Federal Government roughly $90 billion (since the low-yielding loan portfolios return only a portion of book value when sold in today's interest rate environment). It must also be appreciated that the economic loss is not cured by liquidating the institutions; it is far less expensive to keep thrift institutions operating than to trigger that loss through liquidations.

To date, the FSLIC has sought valiantly to avoid liquidations to minimize their expenses while making good on their promise to Federally-insured depositors. Instead, they have pursued a policy of ad hoc restructuring through arranged mergers -- providing guarantees and assistance to the rescuers in amounts less than liquidation costs. Thus, merging these institutions might cut costs to a range of $20 billion to $45 billion. But that assumes that enough merger partners can be found to absorb almost 2,000 institutions. If problems multiply as projected, mergers might soon become no cheaper than actual liquidations. (The FSLIC's sister fund, the FDIC, spent an estimated $1 billion on just five assisted savings bank mergers late last year.) Needless to say, retrenchment of this magnitude implies a very substantial drain on the resources of the FSLIC, which currently maintains reserves of roughly $6 billion.

A recent Washington Post editorial entitled "The Rescue of the S&Ls" summarized well the public policy dilemma:

> "The crucial decision to provide subsidies was taken a long time ago ... when the government began providing deposit insurance. The only question now is the form of the subsidy -- and whether it will be the large amounts that immediate aid will require, or the much larger ones required later to pay off depositors after failure, when the losses will have continued longer."

That the amounts are be large is undisputed. The magnitude of our long-term, fixed-rate mortgage portfolio returning inadequate yields is immense. These are assets of the highest quality -- since families meet their mortgage payments religiously -- but they return too little to compete for savings deposits in today's short-term, high-rate environment. As Exhibit 4 demonstrates, one-third of our assets return less than 9%; approximately two-thirds, less than 10-1/2%; and only one-sixth more than 12%, the approximate level today of 91-day Treasuries. The portfolio "drag" is particularly severe in the Northeast and Midwest, where a legacy of below-market mortgage usury laws is most apparent.

The problems of our institutions and the agencies responsible for the protection of depositors are immediate and serious; equally important is the loss of the product we deliver to the American public, home mortgage loans. The correlation between savings and loan deposit flows and housing activity is direct.

We do not need to catalogue the current state of the housing industry; it is well known to your Subcommittee and the Congress. With mortgage credit too expensive or unavailable, the home construction, realty, lumber and timber, and supplier industries are mired in a deep depression. Unemployment in the construction trades approaches 20%. The ability of the housing sector to lead the country out of recession, as it has done several times since World War II, seems remote -- if unattainable -- as long as savings associations are unable to perform their mortgage finance function.

Families already owning homes are suffering implicit losses, too, thanks to high interest rates. The destruction of the market, as buyers find credit beyond their reach, diminishes the saleability of homes and erodes homeowners' equity.

While we read of other intermediaries coming to the rescue of mortgage finance ... commercial banks, pension funds ... it is abundantly clear that they are either unwilling or unable to do so despite record earnings and effective tax burdens far less than those which apply to thrift institutions. Even with last year's deposit outflows and earnings losses, S&Ls generated $45 billion in mortgage lending -- still considerably more than commercial banks despite their better liquidity and earnings.

The nation needs to preserve the savings and loan business -- the dependable supplier of mortgage credit. This is not to say that the laws and regulations governing our investments today are adequate; they are not. We testified before the Financial Institutions Subcommittee last October that broader asset and liability powers are essential to our future, so that we may achieve the flexibility to sustain us in unstable and hostile economic climates.

Fundamentally, however, savings and loan managers remain committed to doing what they know best -- serving the residential mortgage credit needs of their local communities. They want to stay in that business and perform that service for the American people. They are a vital cog in the housing delivery system.

Unless the Congress acts soon, many thrift institutions will not survive long enough to continue their mission. The real issue is whether the Congress itself, or the regulators acting under duress, will determine the future structure of the nation's financial system. Will a relatively few nationwide depository institutions dominate as survivors, or will the system still include the competition and hometown service of strong, community-oriented thrift institutions?

High interest rates are at the heart of our problem and those of the entire housing industry. We appreciate that the Congress through its Budget process is working diligently to convince the marketplace that your fiscal course is a responsible one and will bring rates down. If interest rates don't come down and stay down, then the savings and loan business will inevitably require substantial financial assistance. We cannot wait for Wall Street to be convinced of the merit of emerging fiscal policy. We need a program put in place immediately. It will be much, much cheaper if rates fall over the next several months and remain down. But, the accumulated damage to date demands some assistance mechanisms right now. If they are not forthcoming, housing and the nation will risk the disappearance of a great and dependable mortgage credit resource.

Chairman St Germain has taken the lead with legislation to preserve the diversity of financial services through his introduction of H.R. 5568, "The Home Mortgage Capital Stability Act". Our organization, in conjunction with the National Association of Mutual Savings Banks, has also been working for several months on a program to sustain our thrift institutions and stimulate home purchase activity at affordable rates.

We hope that H.R. 5568 will provide the framework for Subcommittee and Congressional approval of a temporary and immediate Federal assistance package.

Our joint task force with the savings banks developed a three-part plan: short-term portfolio assistance, short-term capital maintenance, and short-term homebuyer assistance.

The portfolio assistance is aimed at the source of our inability to earn the funds needed to make mortgage loans and pay depositors the rates commanded in today's marketplace for savings. It would permit us to "warehouse" loans in portfolio yielding less than 9% for up to three years through the exchange of those fixed-rate mortgages for the variable-rate notes of an autonomous Government agency. (If these loans were sold outright, institutions would incur an unmanageable loss since current market value is far less than book value.) The notes would carry an interest supplement equal to half the difference between the face rate on the loan "warehoused" and the 30-month constant maturity yield on U.S. Treasury issues (chosen since it relates to today's most popular savings product, the Small Savers Certificate). For example, if an 8% mortgage is exchanged and the 30-month rate was 14% in the preceding calendar quarter, the institution would receive half the difference, 3%, for an 11% return.

Under our plan, the supplement would be suspended whenever the 30-month rate fell below 10%. Homeowner repayments of principal and interest would reduce dollar for dollar the value of loans being warehoused. The "swap" would be reversed at the end of three years. Funding for the temporary supplement would come from Congressionally-authorized appropriations.

To target the assistance where it is needed -- those institutions burdened by the portfolio problem -- eligibility would extend to depositories with 20% or more in assets consisting of residential mortgages (or mortgage-backed securities). This would include some rural and neighborhood commercial banks, as well as savings and loans and mutual savings banks, and perhaps some credit unions. The cost to the Government under this approach depends, of course, on interest rate developments. If Treasury rates remain at mid-February levels (14%), $7.5 billion would be required to "warehouse" the $250 billion in mortgages of less than 9% now held by eligible thrifts and commercial banks. If rates decline, much less would be required. In the case of thrift institutions, the earnings supplement would bring us closer to break-even operations -- and enable us, with the repayment flow on other mortgages and investments, to resume more normal home lending activity. (This statement, however, assumes that further acceleration in the cost of funds does not occur through haphazard actions by the Depository Institutions Deregulation Committee.)

The second portion of our recommended package addresses the deterioration in capital positions (net worth) at depositories. (It is similar to the "net worth guarantee" Chairman St Germain has discussed in public appearances.) Of central importance, this plan would suspend the ad hoc recombination of financial institutions by the regulators -- thus giving the Congress a chance to put the country's fiscal house in order, and Committees such as yours an opportunity to assess the future of depositories in an orderly way (as in your Financial Institutions in a Revolutionary Era project.)

If adopted, it would sustain institutions at a positive 1.5% net worth level through the issuance of Income Capital Certificates. These ICCs are considered net worth by the Federal Home Loan Bank Board, applying Generally-Accepted Accounting Principles. Participation would be open to S&Ls, savings banks, and commercial banks willing to subscribe voluntarily to the program with a nominal stock purchase and annual "user" fees.

The ICCs issued by a participating institution would be exchanged for the promissory notes of an autonomous agency; the notes would carry a guarantee of principal and interest by the U.S. Treasury. On return to profitability (above 1.5% net worth), income brought into net worth would enable the depository to surrender the notes and redeem its ICCs, erasing the Federal assistance.

Dividends accumulated on the ICCs and interest on the promissory notes would accrue at equivalent rates and similarly cancel-out. A cost to the Government, if any, would arise only in the event of liquidation of the institution (in which case the beneficiary of the guarantee would be the FSLIC, FDIC or State liquidating agency). Though a contingent liability is present, there is no immediate Federal outlay. (As mentioned, the skeleton agency involved is capitalized by participating institutions and operated through user fees.)

The first two elements of the assistance package we propose utilize an autonomous government agency, rather than existing supervisory agencies. We make this suggestion for two reasons. First, the plan extends to depositories falling under a number of existing supervisory agencies -- the FDIC, the FSLIC, and, in the case of institutions such as the cooperative banks in New England, State authorities. All share the portfolio and deteriorating capital problems and should be entitled to use the temporary Federal assistance. Secondly, the FSLIC and FDIC's primary orientation is protection of depositors, not preservation of institutions. We would envision that a skeleton agency, similar to the Government National Mortgage Association, could be authorized for these limited portfolio assistance and capital maintenance purposes. It would be self-funding. If necessary, existing agency officials could be installed as board members to maintain continuity with current supervisory activities (as is done with the Federal Home Loan Mortgage Corporation).

Our final recommendation concerns short-term assistance for homebuyers. This program would provide an immediate stimulus to the housing market through an interest-rate "buy-down" available to a broad segment of the homebuying public. We propose that the Treasury (through appopriated funds) and home lending institutions both contribute to this buy-down relief from current mortgage rates. Conventional loans would be available for one year at below-market rates using borrower and mortgage standards patterned after existing HUD middle-income programs (such as the FHA 235 (q)). Lenders would contribute 1% toward the buy-down for the first three years of loan life; the Government would contribute 3% the first year, 2% the second, and 1% the third. (Buy-downs would be calculated from a general market index, such as the FHLMC's composite monthly rate for conventional loans on existing homes.)

Thus, a buyer in a 16.5% mortgage market would be able to obtain a conventional loan at 12.5% at the outset, with the rate changing to 13.5% the following year, and 14.5% the third year. Using the suggested standards, this program could stimulate up to $83.5 billion in home mortgage lending in the coming year -- which would finance about 1.6 million home sales. An estimated $7.5 billion in interest rate relief would be provided to borrowers -- $5 billion (spread over three years) from the Government, and $2.5 billion contributed by participating lenders. This plan should be available for the purchase of both newly-constructed and existing homes -- helping builders, realtors, building tradesmen, suppliers, home sellers, and, of course, families seeking homes.

Our mortgage buy-down assistance recommendation is but one of several put forward recently. It has broad application and a limited life span, consistent with fiscal planning objectives. In connection with your Subcommittee's work, we will also be commenting by separate statement on such excellent initiatives as the multi-family proposal developed by Chairman Gonzalez and Congressman Schumer. We applaud, as well, the Subcommittee's efforts to develop an emergency aid package for homeowners facing foreclosure due to involuntary unemployment, and will be commenting separately on that legislation (H.R. 5598), too.

We also have several observations about Chairman St Germain's welcome and excellent initiative, "The Home Mortgage Capital Stability Act".

As introduced, H.R. 5568 would buttress earnings losses and capital for those institutions, with home loan portfolios comprising at least 20%-of-assets, which have fallen below a 2% net worth-to-assets level for two consecutive quarters. An appropriation of $7.5 billion, not limited to fiscal year, is authorized for this purpose. Existing Federal agencies would administer the assistance and determine whether an "institution demonstrates a need for such assistance and has reasonable prospects for long-term viability".

We would prefer to see the dollar assistance available to all depositories which share the low-yielding, long-term mortgage portfolio burden. That, we feel, is the best and quickest way to restore some normalcy to mortgage lending operations at thrift institutions across America.

Maintaining capital adequacy is vital, too. As we have pointed out, existing regulatory concepts - such as the FHLBB's Income Capital Certificates -- may be adapted to sustain capital at some positive level for all thrift institutions. (The FDIC, however, does not employ the ICC concept.) A Treasury guarantee should attach to the notes exchanged for ICCs (which might be broad enough to encompass stabilization reserves established under quasi-reorganizations of thrift institutions, as well.)

Whatever the agency or agencies chosen to administer a "net worth guarantee" program, we would recommend that they be relieved of such subjective eligibility judgments as a determination of "reasonable prospects for long-term viability" (see Section 2(b)(2)(D) of H.R. 5568). The capricious turns of the interest rate cycles, and such unanticipated outside forces as the haphazard decisions of the Depository Institutions Deregulation Committee, make such long-term assessments very difficult ... if not impossible. That is why our joint task force suggested basically a voluntary subscription mechanism to establish eligibility for capital maintenance. (Our plan does provide, of course, for intervention by existing supervisory authorities through court order if continued operation of a subscriber appears to be grossly negligent or criminal misconduct is involved.)

We also question the housing reinvestment formula set forth in H.R. 5568. As savings and loan associations committed to home finance, we do not object to a home lending obligation _per se_ -- but the formula linking the availability of below-market mortgages to recipients of earnings and capital assistance seems unduly restrictive. We would prefer to see a housing assistance program open to all home lenders, not just as an obligation for those in weakened condition.

In addition, the obligation to issue loans at 1% above the average cost of funds would hinder the ability of assisted institutions to rebuild their earnings and capital positions -- particularly in competition with non-assisted institutions. The bill also ties the loans to an individual institution's cost of funds and is expressed in annual terms. We would suggest that any housing linkage for an assistance program be structured so as to be responsive to general mortgage market conditions (e.g., tied to the FHLMC index) and be flexible enough to keep up with the changes that can occur month-to-month in the mortgage market.

With these few observations, we applaud Chairman St Germain's overall effort and leadership with legislation to halt the shrinkage of our thrift industry and to provide the support needed to begin a housing recovery.

In conclusion, we would like to quote once more from the Washington Post editorial of February 26, 1982:

> "For better or worse, the way this transition works out will set the terms under which you will be able to build, buy, or sell a house for decades to come. A series of bankruptcies in the S&L industry can only make mortgage lending more difficult and expensive."

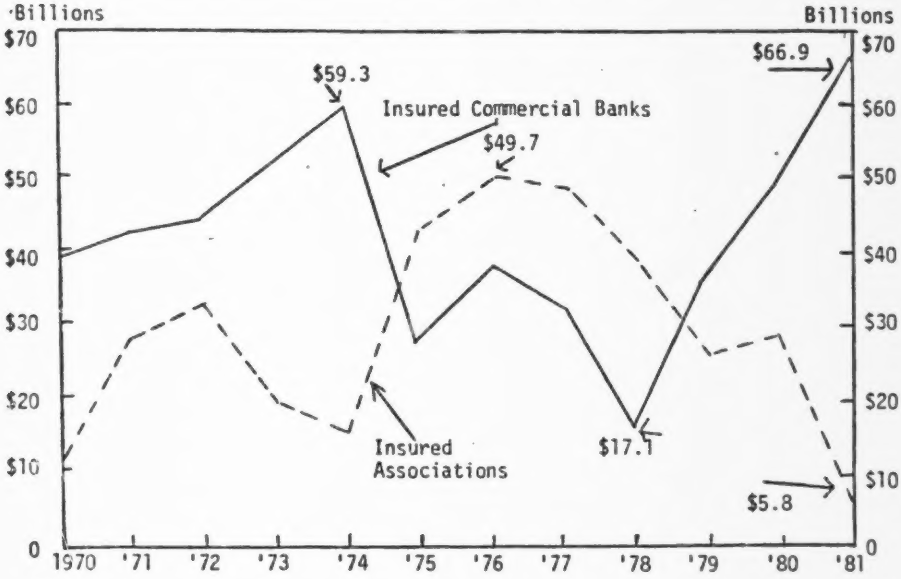
A restored savings and loan business hopes that it may in the future ... as it has so successfully in the past ... join with this Subcommittee in making homeownership a reality for millions of American families.

We appreciated this opportunity to present our views, and we look forward to your questions.

###

EXHIBIT 1

NET SAVINGS GAINS* AT COMMERCIAL BANKS AND SAVINGS ASSOCIATIONS



*Net retail savings gains, 1977-1981

SOURCE: FHLBB, Federal Reserve Board, U.S. League of Savings Associations.

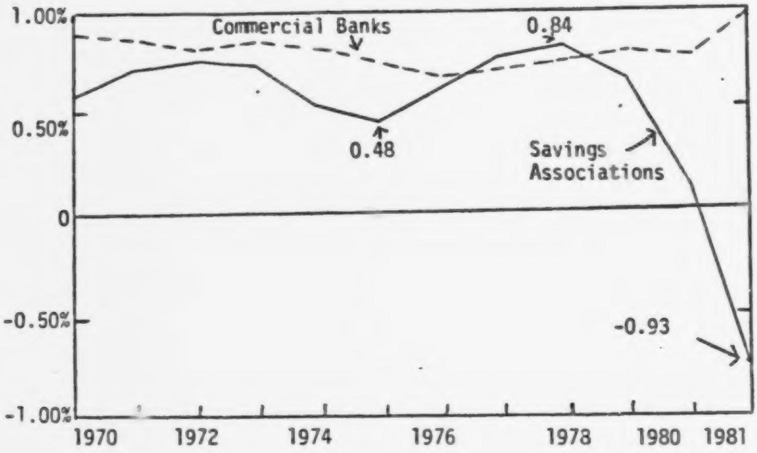
Billions of Dollars

	Insured Commercial Banks	Insured Savings Associations
1970	$38.4	$10.8
1971	41.6	27.3
1972	43.6	32.0
1973	52.0	19.9
1974	59.3	15.6
1975	27.5	42.1
1976	37.7	49.7
1977	32.1	48.0
1978	17.1	38.9
1979	37.3	25.8
1980	49.2	28.4
1981	66.9	5.8

SOURCE: FHLBB, Federal Reserve Board, U.S. League of Savings Assns.

EXHIBIT 2

RETURN ON ASSETS OF COMMERCIAL BANKS AND SAVINGS ASSOCIATIONS



SOURCE: FHLBB, FEDERAL RESERVE BOARD.

	Insured Commercial Banks	Insured Savings Associations
1970	0.90%	0.57%
1971	0.86	0.72
1972	0.83	0.79
1973	0.85	0.77
1974	0.81	0.55
1975	0.77	0.48
1976	0.70	0.64
1977	0.71	0.79
1978	0.76	0.84
1979	0.81	0.68
1980	0.80	0.13
1981	0.98e	-0.93

SOURCE: FHLBB, FEDERAL RESERVE BOARD.

EXHIBIT 3: S&Ls With Less than 2% Net Worth

	LOW RATES*	Ecnonomic Scenario MID RATES*	HIGH RATES*
December, 1982			
Number of Associations	680	1,100	1,350
Assets	$135 B	$ 220 B	$ 290 B
December, 1983			
Number of Associations	1,220	1,800	2,110
Assets	$ 250 B	$ 360 B	$ 420 B

*"Low Rate" = 6 month Treasury Securities at 11.45%
"Mid Rate" = 6 month Treasury Securities at 13.30%
"High Rate" = 6 month Treasury Securities at 14.60%

Source: Research Dept., U.S. League of Savings Associations

EXHIBIT 4

Mortgage Portfolio Structure

Savings and Loan Assns.

As of September, 1981

	$ millions	$ cumulative	%	% cumulative
Under 6%	$6,158	$6,158	1.26%	1.26%
6.00 - 6.49	7,289	13,447	1.49	2.75
6.50 - 6.99	7,187	20,634	1.47	4.22
7.00 - 7.49	17,912	38,546	3.66	7.88
7.50 - 7.99	24,462	63,008	4.99	12.87
8.00 - 8.49	23,769	86,777	4.85	17.72
8.50 - 8.99	76,494	163,271	15.61	33.33
9.00 - 9.49	65,796	229,067	13.43	46.76
9.50 - 9.99	56,560	285,627	11.54	58.30
10.00 -10.49	32,597	318,204	6.65	64.95
10.50 -10.99	31,941	350,145	6.52	71.47
11.00 -11.49	21,213	371,358	4.33	75.80
11.50 -11.99	21,589	392,947	4.41	80.21
12.00 -12.49	18,475	411,424	3.77	83.98
12.50 -12.99	15,819	427,243	3.23	87.21
13.00 -13.49	12,372	439,615	2.52	89.73
13.50 -13.99	9,783	449,398	2.00	91.73
14.00 -14.49	8,654	458,052	1.77	93.50
14.50 -14.99	5,920	463,972	1.21	94.71
15.00 -15.49	5,782	469,754	1.18	95.89
15.50 -15.99	4,150	473,904	0.85	96.74
16.00 -16.49	3,701	477,605	0.76	97.50
16.50 -16.99	2,332	479,937	0.48	97.98
17.00 and over	10,001	489,938 *	2.04	100.00

Nationwide $489,966

* Detail may not add to total because of rounding.

Chairman GONZALEZ. Thank you, sir.

Mr. James Coles, president of the United Savings of Houston, Tex., in his capacity, representing the National Savings & Loan League. Welcome aboard, Mr. Coles.

STATEMENT OF JAMES A. COLES, PRESIDENT OF THE UNITED SAVINGS OF HOUSTON, TEX., AND TREASURER OF THE NATIONAL SAVINGS & LOAN LEAGUE

Mr. COLES. Good morning, Mr. Chairman, and fellow Texan.

Chairman GONZALEZ. Well, you are not from Houston, are you?

Mr. COLES. Yes, sir. That is not as lovely a town as San Antonio, but that is where I make my home.

Chairman GONZALEZ. Well, we will make that a matter of record. [Laughter.] It could be worse, it could be Dallas. [Laughter.]

Mr. COLES. Thank you, Mr. Chairman and members of the subcommittee.

My name is Jim Coles. I am president of the United Savings of Houston and treasurer of the National Savings & Loan League, on whose behalf I appear here today.

On behalf of the membership of the National Savings & Loan League, I first want to thank Chairman St Germain for introducing H.R. 5568, the Home Mortgage Capital Stability Act, which would provide for assistance to depository institutions which are in financial difficulty as a direct result of their commitment to the housing market.

Since the early 1930's, there has been a well understood policy of the Federal Government to assume substantial responsibility for the stability of the Nation's financial intermediary system. The Government further assumes the responsibility of at least encouraging, if not assuring, that there would be a stable supply of credit for housing.

From the creation of deposit insurance, a Federal thrift system, secondary market facilities, and a host of other measures, up to and including the enactment of H.R. 4986, the Congress and in particular, the Banking Committee, has assumed responsibility for the safety and soundness of depository institutions for the security of the deposit insurance funds and for a national housing policy that seeks to maximize the opportunity for homeownership. The bills pending before this subcommitee, H.R. 5568, and H.R. 5731, which was introduced by Chairman Gonzalez, represent a continued commitment to these goals and policies.

The housing and thrift institutions of the Nation's economy are in a near crisis state. While, it is true that the degree of financial stress varies from place to place and from one institution to another, it would be a mistake to assume that the problem is regional in nature. No savings and loan is immune from the effects of paying a higher rate to savers than it receives from borrowers.

The cause of this problem, and its almost unique applicability to thrift institutions, is well understood by this subcommittee. To put it simply, we got into this fix by doing what we were required to do by law, and regulation, and by what we were encouraged to do by public policy. Savings and loans have been, as they were created to be, the primary source of long-term mortgage credit in this country. Beginning about 4 years ago, the market and the Congress told us that we were not paying a fair rate of return to our depositors. Today, market sensitive accounts amount to 65 percent of our deposits.

To date, the solution to the thrift problem, has been to merge institutions. In some cases, with an infusion of capital or with an FSLIC hold harmless guarantee to the acquiring institution against losses from the low-yield assets of the acquired thrift.

The administration has refused to consider any direct assistance to thrifts, preferring to rely on the merger process. The administration and the Congress, by silence, also seemed to imply that the merger solution is cost free.

Even if the merger process could go on indefinitely, the cost would be high. Far from a no-cost solution, the present course of action is potentially a very costly one. If the estimate of 1,000 thrifts being merged out over the next few years is reasonably accurate, we believe that the resources of the FSLIC will be severely strained.

We do not believe that the merger process, by itself, is a viable solution. While the merger process has been successful in avoiding the worst of all outcomes, liquidation, it has clearly not done the job in terms of restoring public confidence. Virtually every supervisory merger has been headlined in the press as a failure. The supervisory mergers have had an adverse affect on the public's confidence in thrift institutions generally, as evidenced by the $25.4 billion savings outflow in 1981, compared to a $10.7 billion inflow, in the previous year. Public confidence in the whole structure of the thrift industry is very much at issue here, today, and ultimately in the public's confidence in the Nation's financial system.

H.R. 5568, the Home Mortgage Capital Stability Act, introduced on February 23, by Chairman St Germain, would provide for a $7.5 billion pool of money, at the Treasury, from which the financial regulatory agencies could draw to assist financially troubled institutions under their supervision.

The bill provides minimal requirements for the eligibility of institutions for financial assistance with a great deal of discretion left up to the regulators. The latter point, is in our view, the most important in terms of who gets the help. Before the FSLIC grants the assistance, it must be reasonably sure of the long-term viability of the savings and loan association in question.

The financial assistance available to institutions selected by the FSLIC would take two forms. First, the FSLIC would use the funds to purchase capital notes from the institutions in amounts to raise the net worth to 2 percent. Subsequently, the FSLIC would make payments to the institutions in amounts equal to their operating losses to maintain net worth at 2 percent.

Given the broad grant of authority to the Federal Home Loan Bank Board to pick and choose who gets the assistance we respectfully suggest that the 2 percent net worth test is unnecessarily rigid. We hope the subcommittee will consider giving the regulators the authority to extend these earnings stabilization payments onto the same terms and conditions to otherwise qualified institutions whose net worth is declining, but still in excess of 2 percent.

The National League, supports the principle of a continued commitment to housing by institutions receiving short-term assistance from the HMCS fund. We do believe, however, that this provison of H.R. 5568 is written too narrowly.

The institutions should have the flexibility to meet the housing credit needs of their community, by as well, making home improvement loans, loans for the rehabilitation of older structures, and loans for mobile homes.

MORTGAGE WAREHOUSING

Mr. Chairman, the inability of thrift institutions to maintain financial health and profitability in the current interest rate environment is very simply, caused by large portfolios of long-term, low-yield mortgage assets.

One of the mechanisms for temporary relief, therefore, which we would urge this subcommittee to consider as a supplement to H.R. 5568, is a temporary mortgage warehousing plan. The broad outline of a warehousing plan can be found in H.R. 5030 introduced last year by Representative John LaFalce, a member of the House Banking Committee.

An eligible institution would be permitted to exchange a portion of its 9 percent or less mortgages, for a variable rate notes issued by the FSLIC, or the FDIC, with rates tied to Treasury Bill rates. The difference between the yields would, in effect, be an earnings maintenance loan, to be fully repaid over a 3 to 5 year period.

Mr. Chairman, members of the subcommittee, we are very much aware that there could not be a worse time to come here and ask you to enact legislation which adds to the overall budget deficit. We would not do so, if we were convinced that there were any reasonable short-term alternatives. In our judgment, doing nothing now and allowing a continued erosion of the financial condition of a substantial part of our depository system runs the risk of much more expensive, less controllable costs in the months and years ahead. While the deposit insurance funds are sound today, Congress must address the issue of how much more pressure can be permitted on the insurance funds. That is a judgment that you must make.

Members of the committee, I thank you for the opportunity to appear before you today, and I look forward to your questions.

[The prepared statement of Mr. Coles, on behalf of the National Savings & Loan League, follows:]

TESTIMONY OF
JAMES A. COLES
ON BEHALF OF
THE NATIONAL SAVINGS AND LOAN LEAGUE

ON HR 5568

BEFORE THE
SUBCOMMITTEE ON HOUSING AND
COMMUNITY DEVELOPMENT
U. S. HOUSE OF REPRESENTATIVES

MARCH 18, 1982

Mr. Chairman, Members of the Subcommittee, my name is James A. Coles. I am President of United Savings of Houston, Texas, and Treasurer of the National Savings and Loan League on whose behalf I appear here today. The National League appreciates this opportunity to express the concern we feel for the future of the mortgage credit delivery system of this country and the future of housing and homeownership.

On behalf of the membership of the National Savings and Loan League, I first want to thank Chairman St Germain for introducing H.R. 5568, the "Home Mortgage Capital Stability Act," which would provide for financial assistance to financial institutions which are in financial difficulty as a direct result of their commitment to the housing market. We are pleased to be able to announce here today our support for the bill. We will, however, suggest a few specific amendments to the bill as well as a supplemental financial assistance plan aimed directly at the core of the thrifts' current financial problem.

Before discussing the specifics of H.R. 5568, a few general observations about housing policy are, we think, in order. Since the early 1930s there has been a well understood policy of the federal government to assume substantial responsibility for the stability of the nation's financial intermediary system. The government further assumed the responsibility of at least encouraging, if not assuring, that there would be a stable supply of credit for housing. These policies have at times been explicit--at other times, implicit--in actions taken by Congress over the last fifty years. From the creation of deposit insurance, a federal thrift system, secondary market facilities, and a host of other measures, up to and including the enactment of H.R. 4986, the Congress, and in particular the Banking Committee, has assumed responsibility for the safety and soundness of depository institutions, for the security of the deposit insurance funds, and for a national housing policy that seeks to maximize the opportunity for homeownership.

The bills pending before this Subcommittee, H.R. 5568 and H.R. 5731 which was introduced by Chairman Gonzalez, represent a continued commitment to these goals and policies.

Both bills are directly related to the issue of a national housing policy. The goal of decent, affordable housing and a suitable living environment has been an implicit, if not explicit, policy of the federal government for fifty years. It is fair, we think, to ask today whether or not this remains our national policy. It is fair, we suggest, to ask the Congress and the Administration to answer that question explicitly to the American people.

The housing and thrift industry components of the nation's economy are in a near-crisis state with interest rates pricing all but the most affluent people out of housing, production below one million units per year, virtually no rental construction in many cities where it is desperately needed, and unemployment in the construction trades rising.

The savings and loan industry--taken as a whole--lost about $5 billion in 1981, reducing the combined net worth or reserves of the industry from $32 billion a year ago to approximately $27 billion today. While it is true that the degree of financial stress varies from place to place and from one institution to another, it would be a mistake to assume that the problem is regional in nature. No savings and loan is immune from the effects of paying a higher rate to savers than it receives from borrowers. The losses that result eat away at the institution's net worth.

The cause of this problem--and its almost unique applicability to thrift institutions--is well understood by this

Subcommittee, but apparently is not understood elsewhere. To put it simply, we got into this fix by doing what we were required to do by law and regulation, and by what we were encouraged to do by public policy. Savings and loans have been, as they were created to be, the primary source of long-term mortgage credit in this country. They have provided mortgage credit in the form of long-term, fixed-rate loans.

Beginning about four years ago, the market and the Congress told us we were not paying a fair rate of return to our depositors. As a result, market-sensitive instruments were created to stem disintermediation and "give the saver a fair shake." In this hearing room two years ago, we were severely chastised for objecting to a five-year phase-out of rate ceilings on savings. Well, we have been paying an increasingly higher rate and an increasingly volatile rate on savings. The net result is we hold the 6, 8, and 10% fixed rate loans the government wanted us to make, and we are paying our depositors an average rate of 11½% while the average yield on our mortgages is 10%. Market sensitive savings accounts amount to 65% of our deposits today.

To date, the "solution" to the thrift problem has been to merge institutions in some cases with an infusion of capital or with an FSLIC "hold harmless" guarantee to the acquiring institution against losses from the low-yield assets of the acquired thrift. The Administration has refused to consider any direct assistance to thrifts--preferring to rely on the merger process. They seem to assume that, in time, the problem will go away--i.e. that the thrifts will be merged out quietly until interest rates fall and the problem solves itself. The Administration and the Congress by their silence also seem to imply that the merger solution is cost free. Both assumptions are in error. The problem isn't going away. In 1981 there were three FDIC-assisted mergers and 23 FSLIC assisted mergers costing each agency about $1 billion. The potential cost to FSLIC from its previous commitments and from the future mergers it will be required to arrange will be even more costly.

It may well be, Mr. Chairman, that some substantial degree of consolidation of the depository system is inevitable--given marketplace changes, technological innovations, and changes in consumer demands and expectations for financial services. One could argue that this consolidation would eventually affect all segments of the depository network. We are, therefore, prepared to accept the notion that a restructuring of the system and a degree of consolidation is inevitable, but the process of "natural selection" that would occur in a stable economic environment will not be achieved in the present climate.

Even if the merger process could go on indefinitely, the costs would be high. Assisted mergers may very well require direct financial infusion from Treasury. Far from a no-cost solution, the present course of action is potentially a very costly solution. If the estimate of 1,000 thrifts being merged out over the next few years is reasonably accurate, we believe that the resources of the FSLIC will be severely strained.

We do not believe that the merger process by itself is a viable solution. While the merger process has been successful in avoiding the worst of all outcomes--liquidation of insured institutions--it has clearly not done the job in terms of restoring public confidence. Virtually every supervisory merger has been headlined in the press as a failure. The supervisory mergers have had an adverse effect on the public's confidence in thrift institutions generally as evidenced by the $25.4 billion savings outflow we experienced in 1981 compared to a $10.7 billion inflow in 1980.

Public confidence in the whole structure of the thrift industry is very much at issue here, and ultimately in the public's confidence in the nation's financial system.

It should be obvious that the current interest rate environment will make near-term profitability impossible. Indeed, if rates stay where they are, 1982 will be as bad or worse than 1981. If there were any reasonable expectation that interest rates would decline sharply to say a 6-month MMC rate of 8% and a 30-month rate of 10% and stay there, WE WOULD NOT BE HERE TODAY!

We are willing to accept on faith that the Congress and the President will somehow get the government's fiscal house in order, which is the ultimate and only permanent solution to our problems. We can, however, no longer wait for that to occur. While we would prefer to work out our problems through our own means rather than coming to Congress to ask for direct assistance that will have a short-term negative budget impact, we have come to the conclusion that we have no other choice.

H.R. 5568

The Home Mortgage Capital Stability Act introduced on February 23 by Chairman St Germain would provide for a $7.5 billion pool of money at the Treasury from which the financial regulatory agencies could draw to assist financially troubled institutions under their supervision.

The bill provides minimal requirements for the eligibility of institutions for financial assistance with a great deal of discretion left to the regulators. The latter point is, in our view, the most important in terms of who gets the help. Before the FSLIC grants the assistance, it must be reasonably sure of the "long-term viability" of the savings and loan in question. In other words, the bill puts the FSLIC in the position of deciding who is worth saving and who isn't.

The financial assistance available to institutions selected by the FSLIC would take two forms: raising an institution's net worth to 2% and maintaining it at that level.

First, the FSLIC would use the funds to purchase capital notes from the institutions in such amounts to raise the net worth to 2%. Subsequently the FSLIC would, on a quarterly basis, make payments to the institutions in amounts equal to their operating losses to maintain net worth at the 2% level.

Given the broad grant of authority to the FHLBB to pick and choose who gets the assistance, we respectfully suggest that the 2% net worth test is unnecessarily rigid. We hope the Subcommittee will consider giving the regulators the authority to extend "earnings stabilization payments" (under the same terms and conditions) to otherwise qualified institutions whose net worth is declining but still above 2%.

Financial assistance received under this program would be repaid to the Treasury (at a rate of interest to be set by the Secretary) after the assisted institution has rebuilt its net worth to 3%, or after five years. The repayment schedule calls for 50% of after-tax profit to be committed to redeeming the capital notes and earnings stabilization payments. Since repayments from the qualifying institutions will go directly into the HMCS Fund at the Treasury, it will be a revolving fund.

As a result, the initial cost to the government is controllable and, in the long run, the cost will be zero.

From the time that an institution begins receiving assistance to the time that the assistance is fully repaid to the Fund, the institution would be obligated to commit 50% of its deposit growth to residential mortgages for first-time homebuyers in amounts not greater than the FHA limit and at interest rates of 1% over the institution's average cost of funds. Up to one-half of this obligation could be met through the purchase of securities backed by mortgages meeting these same qualifications.

The National League supports the principle of a continued commitment to housing by institutions receiving short-term assistance from the HMCS fund. We strongly believe, however, that the requirement is written far too narrowly. Institutions should have the flexibility to meet the housing credit needs of their community by also making home improvement loans, loans for the rehabilitation of older structures, and loans for mobile homes.

We also would urge the Subcommittee to provide regulatory latitude on the permissible interest rate limit on qualifying loans. The commitment of 50% net new funds is a reasonable standard, but the rate of interest should be tied to these funds (i.e. the marginal cost of funds) rather than the cost of funds already on deposit and already committed to existing loans. Given the rigidity of this requirement as it is now written, we believe the government will end up perpetuating the depressed earnings condition of the associations getting the assistance.

Mortgage Warehousing

Mr. Chairman, the inability of thrift institutions to maintain financial health and profitability in the current interest rate environment is, very simply, caused by large portfolios of long-term, low-yield mortgage assets. One of the mechanisms for temporary relief, therefore, which we would urge this Subcommittee to consider as a supplement to H.R. 5568, is a temporary mortgage warehousing plan.

The broad outline of a warehousing plan can be found in H.R. 5030 introduced last year by Rep. John La Falce, a member of the House Banking Committee. An eligible institution would be permitted to exchange a portion of its 9% or less mortgages for variable-rate notes issued by the FSLIC or the FDIC with rates tied to Treasury bill rates. The difference between the yields would in effect be an earnings maintenance loan to be fully repaid over a three- to five-year period. In the long run, this approach involves no cost to the government. In the short run, there is a budget impact which would be variable with the rise or fall of interest rates generally. The initial funds for the interest rate spread on the assets to be exchanged could come from the HMCS Fund called for in H.R. 5568 or a similarly appropriated fund. Alternatively these funds could be raised by authorizing the FSLIC to borrow with the full faith and credit of the United States. The terms and conditions can be closely linked. Consultation with the Secretary of the Treasury in setting these terms and conditions would be an appropriate legislative safeguard.

We recommend that the FSLIC be given the authority to use the warehousing fund for any insured institution experiencing sustained losses regardless of current net worth. We also suggest that the redemption terms be set by the FSLIC with appropriate reporting requirements to the Congress and the Treasury Secretary.

Conclusion

Mr. Chairman, Members of the Subcommittee, we are very much aware that there couldn't be a worse time to come here and ask you to enact legislation which adds to the overall budget deficit. We would not do so if we were convinced that there were any reasonable short-term alternatives. In our judgment, doing nothing now and allowing a continued erosion of the financial condition of a substantial part of our depository system runs the risk of much more expensive, less controllable costs in the months ahead. While the deposit insurance funds are sound today, Congress must address the issue of how much more pressure can be permitted on the insurance funds. That is a judgment you must make.

Thank you for the opportunity to appear before you today. I look forward to your questions.

Chairman GONZALEZ. Thank you very much, sir. The next witness is William B. Muse, Jr., the president of Imperial Savings & Loan Association, Martinsville, Va., representing the American Savings & Loan League.

STATEMENT OF WILLIAM B. MUSE, JR., PRESIDENT OF IMPERIAL SAVINGS & LOAN ASSOCIATION, MARTINSVILLE, VA., REPRESENTING THE AMERICAN SAVINGS & LOAN LEAGUE, INC.

Mr. MUSE. Thank you, Mr. Chairman. It is a great pleasure to be here, particularly to hear the comments of the members of the subcommittee who have expressed their concern for the problems which we are addressing today.

I am here as a member of the legislative committee of the American Savings & Loan League, and I am president of Imperial Savings & Loan Association of Martinsville, Va. I am pleased to present to you the views of the American Savings & Loan League on H.R. 5568, a measure concerned with maintaining the net worth of mortgage issuing depository institutions above the 2-percent mark.

The ASLL's members are savings associations owned or controlled by blacks, Hispanics, and Asian Americans. Our associations are small and young; most of us have less than $100 million in assets and only one-half have been in existence for more than 10 years.

In spite of our small size, however, our institutions have become an integral part of minority neighborhoods throughout the country. Collectively we represent over $2.6 billion in assets.

These assets are for the most part mortgages we have been able to make for minority homeownership. ASLL members provide mortgage financing for inner city homeowners. We help alleviate urban blight by investing in minority economic development activities; and by the mere fact of our existence, we serve as role models to boost the morale of other members of the minority business community.

Presently, economic forces combined with the total insensitivity of the Reagan administration are threatening the survival of minority thrift institutions. Some of the problems of minority S. & L.'s are common to the entire thrift industry.

The major problem we have in common is declining net worth due to the high cost of short-term borrowing. According to the Federal Home Loan Bank Board, the national average cost of funds for FSLIC-insured associations for the 6 months ending June 30, 1981, was 10.31 percent. The portfolio yield for the same period was 9.27 percent. This represents a negative spread of 0.59 percent. Statistics for the second half of 1981 show that the negative spread has increased. Accordingly, out of 79 minority S. & L.'s, 51 posted net operating losses for the year, ranging from $1,702 to $1,950,394. We were able to absorb last year's losses by our accumulated surplus. However, should this negative spread continue to erode the net worth of the industry, many S. & L.'s soon will not be able to maintain the required statutory reserves. I am sure that the committee knows of the number of S. & L.'s that are projected to disappear if the current conditions continue.

Minority S. & L.'s have some distinct problems of their own. In the marketplace we are disadvantaged by size; and the disposable incomes of our depositors are less, causing them to have lower balances and more active accounts that are more costly for us to maintain.

Further, our size does not allow us to benefit fully from the new investment powers recently granted to the savings and loan industry. In contrast to older S. & L.'s, one-half of our member institutions have not had sufficient time to accumulate adequate net worth and develop a broad customer base.

This situation has been exacerbated by several recessions since 1974 and current economic conditions. Today, the survival of minority S. & L.'s is seriously threatened, since the solutions to low net worth usually is merger with a larger, stronger, but nonminority institution.

Over the past year and a half, seven American League members have been merged out of existence because of inadequate net worth. Without some form of assistance to shore up the net worth of the remaining associations, we can be sure to see many more mergers with disastrous consequences for minority S.& L.'s and the communities they were chartered to serve.

Public confidence in our areas is a very important thing. Without that confidence in our cities, you would create other problems. Without doubt, their loss will be felt by their communities, as minority S. & L.'s are frequently the only financial presence in inner-city neighborhoods. Their efforts, however small, have been directed toward promoting homeownership among minorities and toward slowing the process of urban decay. For years we were the only consistent mortgage lenders in "redlined" inner city areas. Finally, these minority institutions have set an example which may convince the younger generation of black, Hispanics, and Asian Americans that the American dream can work for them too.

Today, however, the situation is sufficiently serious to warrant concern that the very phenomenon of minority savings and loan association is facing extinction. The St Germain bill will help maintain the strength and viability of minority S. & L.'s, and help us weather the current economic storm. It is a timely measure, for the public confidence in the savings and loan industry is beginning to decline. Articles with provocative titles such as, "How Safe Are Your Savings?" appear in the press almost daily, causing depositors to worry about the viability of the thrift industry.

The edifice of the banking system, painstakingly built on the public confidence in the aftermath of the great runs on banks in the early 1930's, may crumble unless the authorities evince strong commitments to back up the thrift industry. The repercussions will definitely spread into the banking industry, and the consequences for the economy as a whole will doubtless be serious.

We support the Home Mortgage Capital Stability Act because it is a timely remedy for the thrift industry as a whole. Moreover, we have a particular desire to see the bill pass, for the assistance is not partial to big associations, but is committed to save any viable mortgage-lending depository institution, regardless of its size.

This would assure that the standard of fairness is maintained and would have the added benefit of preserving the separate identity of the minority S. & L. Whether governmental assistance will come in the form of a capital stability fund, net worth guarantee, or some combination of the two, it will be a long overdue measure to relieve the burdens on our industry. Therefore, the American Savings & Loan League supports this proposal and would urge its speedy enactment.

I would be pleased to respond to any questions that you might have.

[Mr. Muse's prepared statement, on behalf of the American Savings & Loan League, Inc., follows:]

STATEMENT OF WILLIAM B. MUSE, JR.
PRESIDENT
IMPERIAL SAVINGS AND LOAN ASSOCIATION
MARTINSVILLE, VIRGINIA

ON BEHALF OF

THE AMERICAN SAVINGS AND LOAN LEAGUE, INC.
March 18, 1982

Mr. Chairman and Members of the Committee, I am William B. Muse, President of Imperial S&LA of Martinsville, Virginia. I am pleased to present to you the views of the American Savings and Loan League on H.R. 5568, a measure concerned with keeping the net worth of mortgage-issuing depository institutions above the two-percent mark.

The ASLL's members are savings associations owned or controlled by Blacks, Hispanics, and Asian-Americans. Our associations are small and young; most of us have less than $100 million in assets and only one-half have been in existence for more than 10 years. In spite of our small size, however, our institutions have become an integral part of minority neighborhoods throughout the country. Collectively we represent over $2.0 billion in assets. These assets are for the most part mortgages we have been able to make for minority homeownership. We provide mortgage financing for inner-city homeowners. We help alleviate urban blight by investing in minority economic development activities; and by the mere fact of our existence, we serve as role models to boost the morale of other members of the minority business community.

PResently, economic forces combined with the total insensitivity of the Reagan Administration are threatening the survival of minority thrift institutions. Some of the problems of minority S&Ls are common to the entire thrift industry. The major problem we have in common is declining net worth due to the high cost of short-term borrowing. According to the Federal Home Loan Bank Board, the national average cost of funds for FSLIC-insured associations for the six months ending June 30, 1981, was 10.31 percent. The portfolio yield for the same period was 9.27%. This represents a negative spread of 0.59%. Statistics for the second half of 1981 show that the negative spread has increased. Accordingly, out of 79 minority S&Ls, 51 posted net operating losses for the year, ranging from $1,702 to $1,950,394. We were able to absorb last year's losses by our accumulated surplus. However, should this negative spread continue to erode the net worth of the industry, many S&Ls soon will not be able to maintain the required statutory reserves. I am sure the Committee knows of the number of S&Ls that are projected to disappear if current conditions continue.

Minority S&Ls have some distinct problems of their own. In the marketplace we are disadvantaged by size; the disposable incomes of our depositors are less, causing them to have lower balances and more active accounts that are costly for us to maintain. Further, our size does not allow us to benefit fully from the new investment powers recently granted to the savings and loan industry. In contrast to older S&Ls, one-half of our member institutions have not had sufficient time to accumulate adequate net worth and develop at broad customer base. This situation has been exacerbated by several recessions since 1974 and current economic conditions. Today, the survival of minority S&Ls is seriously threatened, since the solution to low net worth usually is merger with a larger, stronger, but non-minority institution. Over the past year and a half, 7 American League members have been merged out of existence because of inadequate net worth. Without some form of assistance to shore up the net worth of the remaining associations, we can be sure to see many more mergers with disastrous consequences for minority S&Ls and the communities they were chartered to serve. Without doubt, their loss will be felt by their communities, as minority S&Ls are frequently the only financial presence in inner-city neighborhoods. Their efforts, however small, have been directed toward promoting homeownership among minorities and toward slowing the process of urban decay. For years they had been the only consistent mortgage lenders in "redlined" inner-city areas. Finally, these minority institutions have set an example which may convince the younger generation of Blacks, Hispanics and Asian-Americans that the American dream can work for them too.

Today, however, the situation is sufficiently serious to warrant concern that the very phenomenon of minority savings and loan association is facing extinction.

The St. Germain bill will help maintain the strength and viability of minority S&Ls, and help us weather the current economic storm. It is a timely measure, for the public confidence in the savings and loan industry is beginning to decline. Articles with provocative titles such as, "How Safe Are Your Savings?" appear in the press almost daily, causing depositors to worry about the viability of the thrift industry. The edifice of the banking system, painstakingly built on the public confidence in the aftermath of the great runs on banks in the early Thirties, may crumble unless the authorities evince strong commitments to back up the thrift industry. The repercussions will definitely spread into the banking industry, and the consequences for the economy as a whole will doubtless be serious.

We support the Home Mortgage Capital Stability Act because it is a timely remedy for the thrift industry as a whole. Moreover, we have a particular desire to see the bill pass, for the assistance is not partial to big associations, but is committed to save any viable mortgage-lending depository institution regardless of its size. This would assure that the standard of fairness is maintained and would have the added benefit of preserving the separate identity of the minority S&L. Whether governmental assistance will come in the form of a capital stability fund, net worth guarantee, or some combination of the two, it will be a long overdue measure to relieve the burdens on our industry. Therefore, the American Savings and Loan League supports this proposal and would urge its speedy enactment.

I would be pleased to respond to any questions you might have.

Chairman GONZALEZ. Thank you, Mr. Muse. And thank you, gentlemen. We will proceed under the 5-minute rule, even though I will try to not utilize 5 minutes because we are taking advantage of the hearings that we announced at the subcommittee level on housing to process the hearing on the chairman's bill, that actually comes out of his subcommittee that he chairs and has chaired for a long time. And I certainly am supportive. I cannot help but be.

On the other hand, I must be fair to myself, because it seems to me that the real solution to this situation is a lot more complex than this emergency approach.

We reached this point, where it is tragic and we should be resorting to emergency, because usually when we react in an emergency we do not react comprehensively, too wisely, or too prudently.

And I hope that I am wrong, but I do not think that it is different in this case. We had in the subcommittee, common events cast their shadows before. When we had the original big disintermediation, in the credit crunch of 1966, subsequent to that period, we had the Hunt Commission, we had defined studies, and then everyone of those recommendations, of course, we could not get agreement, there was no consensus, as you will remember.

Then I saw with alarm, what we did 2 years ago, 3 years ago, not only in this area of banking. But we got into this deregulatory mania. I call it a mania, because it was like a jogging fad here. And I found myself very lonely, very lonely, protesting in the name of deregulation the death knell, what was obvious to me, of those that were the objectives of protection in the sense of equality of struggle, some chance to get into the ring and have some kind of a balanced fight, actually being forgotten.

And as it has turned out, tragically, I think that I was right. Whether it was the deregulation of the airlines, which the Congress did not directly affect, which was done through administrative fiat, but more particularly in the deregulatory act of the trucking industry, the railroad industry, our voices were drowned out.

The only thing that we could do was to make a Congressional Record for legislative purposes, anticipating that there would be some judicial contest, down the line.

When we had the so-called Banking Deregulatory Act, the Bank Reform Act, and all, and created what I think that many of you are asking now, to either modify or do away with the so-called deregulatory interagency deregulatory body. The Congress, in my opinion, was shifting its responsibility over to them.

And the reason being, that for my skepticism, that it looked as if, what we were doing indirectly, was accomplishing some of those aims and objectives that had been recommended—the unitary regulatory in the case of banking and financial institutions envisioned with no decision as to just how, these smaller members or these weaker members could be defended against encroachment.

So now we have go mergers, as what? As an emergency to do what? To bookkeeping wise, keep institutions alive which probably would have gone under or will go under. The fundamental policy is still, I think, staring us in the face. I do not see how in the world we can really, really help. The reason as I say that I must be supportive of this is that you do have your housing tie-in. But that in itself is what the burden of recommendation of modification is, in your presentations.

What I am trying to say, is that I am afraid that the only real way that the help in time to save whatever is savable now, would be to find a method either through the Government or through some other way, to just take off your low-yielding responsibilities. I do not see how else it is going to be done. We are just kidding ourselves. We have gone through all of this gimmickery for 1 year.

All-savers certificate, that came to us indirectly through the tax bill. Nobody was saying anything because I think that even your industry got lost in the good old American dream that you could triumph and not realizing that you were going to be put in competition with the real giants.

It was like getting a light-weight to go into the ring with Muhammad Ali. You do not have to be a prophet to know what is going to happen. So at this point the only thing that I see, and I do not say this disrespectfully of the efforts that are being made, because I think that our chairman is to be commended, that is the one last good hope.

But, I think that we ought to be honest with ourselves, too. So, actually it would lead to a specific question that I will submit in writing to the panel in time for you to perhaps answer it in the transcript when you receive it.

And that is, how we can assure that even if these things work, that the lion's share of mortgages move aggressively into this area of housing.

I recognize Mr. Stanton, my time has expired.

Mr. STANTON. Thank you, Mr. Chairman. Gentlemen, I apologize for being called out a couple of times.

I have not had an opportunity, to be truthful, to read all of these statements from all of these institutions. I have read two of them last night, and the other two of them, I certainly will read. In that regard, Mr. Chairman, our minority staff has a total of about 10 pages here of individual questions, divided up into the different panelists. I wonder if, for the record, we could just submit these questions and then have the participants, at their leisure, fill in the answers that are of concern to our staff.

Chairman GONZALEZ. Without objection, so ordered.

[The following correspondence containing additional questions was sent to the witnesses and appears with the response of the witnesses:]

FERNAND J. ST GERMAIN, R.I., CHAIRMAN
HENRY S. REUSS, WIS.
HENRY B. GONZALEZ, TEX.
JOSEPH G. MINISH, N.J.
FRANK ANNUNZIO, ILL.
PARREN J. MITCHELL, MD.
WALTER E. FAUNTROY, D.C.
STEPHEN L. NEAL, N.C.
JERRY M. PATTERSON, CALIF.
JAMES J. BLANCHARD, MICH.
CARROLL HUBBARD, JR., KY.
JOHN J. LAFALCE, N.Y.
DAVID W. EVANS, IND.
NORMAN E. D'AMOURS, N.H.
STANLEY N. LUNDINE, N.Y.
MARY ROSE OAKAR, OHIO
JIM MATTOX, TEX.
BRUCE F. VENTO, MINN.
DOUG BARNARD, JR., GA.
ROBERT GARCIA, N.Y.
MIKE LOWRY, WASH.
CHARLES E. SCHUMER, N.Y.
BARNEY FRANK, MASS.
BILL PATMAN, TEX.
WILLIAM J. COYNE, PA.
STENY H. HOYER, MD.

U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
NINETY-SEVENTH CONGRESS
2129 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515

J. WILLIAM STANTON, OHIO
CHALMERS P. WYLIE, OHIO
STEWART B. MCKINNEY, CONN.
GEORGE HANSEN, IDAHO
JIM LEACH, IOWA
THOMAS B. EVANS, JR., DEL.
RON PAUL, TEX.
ED BETHUNE, ARK.
NORMAN D. SHUMWAY, CALIF.
STAN PARRIS, VA.
ED WEBER, OHIO
BILL McCOLLUM, FLA.
GREGORY W. CARMAN, N.Y.
GEORGE C. WORTLEY, N.Y.
MARGE ROUKEMA, N.J.
BILL LOWERY, CALIF.
JAMES K. COYNE, PA.
DOUGLAS K. BEREUTER, NEBR.
DAVID DREIER, CALIF.
225-4247

April 6, 1982

Mr. Jonathan Lindley
Executive Vice President
National Savings and Loan League
1101 Fifteenth Street, N. W., Suite 400
Washington, D. C. 20005

Dear Jonathan:

Your recent testimony on H.R. 5568, the Home Mortgage Capital Stability Act, before the Subcommittee on Housing and Community Development has been received with great interest and studied closely by Minority Members and Committee staff.

Unfortunately, the limited amount of time available at the hearings did not permit as full a discussion of the issues as we would have liked. However, the Minority staff has developed a series of questions designed to give the witnesses a fuller opportunity to present their views for the record.

It would be very helpful, therefore, if you would respond to the attached list of questions. In order to ensure that your answers will be included in the hearing record, they should be received no later than April 16.

Thank you for your cooperation.

Sincerely,

J. William Stanton

JWS:bfd

Attachment

QUESTIONS FOR MR. COLES:

1. ON PAGE 3 YOU REFER TO THE FACT THAT THE INDUSTRY AS A WHOLE HAS A NET WORTH OF $27 BILLION. CHAIRMAN PRATT HAS TESTIFIED THAT IN THE THIRD QUARTER OF 1981, THE SHARE OF MORTGAGE LENDING ACCOUNTED FOR BY SAVINGS AND LOAN ASSOCIATIONS WAS ONLY 8 PERCENT. (PAGE 9 OF CHAIRMAN PRATT'S STATEMENT.)

WITH ALLOWANCE FOR SOME FURTHER DECREASE, DOES THIS TOTAL INDUSTRY NET WORTH NOT DEFINE FAIRLY WELL THE EXTENT TO WHICH THE INDUSTRY CAN PARTICIPATE IN HOUSING FINANCE, REGARDLESS OF THE NUMBER OF INSTITUTIONS WHICH PARTICIPATE IN THE INDUSTRY IN THE FUTURE?

2. ON PAGE 5 YOU STATE, "WE ARE, ..., PREPARED TO ACCEPT THE NOTION THAT A RESTRUCTURING OF THE SYSTEM AND A DEGREE OF CONSOLIDATION IS INEVITABLE, BUT THE PROCESS OF 'NATURAL SELECTION' THAT WOULD OCCUR IN A STABLE ECONOMIC ENVIRONMENT WILL NOT BE ACHIEVED IN THE PRESENT CLIMATE."

CHAIRMAN PRATT HAS TESTIFIED THAT, "SHOULD FEDERAL INTERVENTION OCCUR, IT SHOULD BE STRUCTURED IN SUCH A WAY THAT IT IS MARKET-DISCIPLINED, EFFICIENT TO ADMINISTER, AND DARWINIAN IN IMPACT, ALLOWING THE WEAKEST MEMBERS OF THE INDUSTRY TO GO OUT OF EXISTENCE, WHILE PRESERVING THE STRONGER INSTITUTIONS." (PAGE 16 OF CHAIRMAN PRATT'S STATEMENT.)

IS IT NOT EQUALLY LIKELY THAT THE NATURAL SELECTION PROCESS COULD FUNCTION MORE EFFICIENTLY IN THE PRESENT ENVIRONMENT THAN IT WOULD AFTER THE ADMINISTRATION OF A MASSIVE ASSISTANCE PROGRAM DESIGNED TO FORESTALL THE ATTRITION WHICH WOULD OTHERWISE OCCUR?

DO YOU SEE ANY DANGER THAT THE PROVISION OF FEDERAL ASSISTANCE TO TROUBLED INSTITUTIONS, BY ENABLING THESE INSTITUTIONS TO CONTINUE TO EXIST, OR TO COMPETE MORE VIGOROUSLY THAN THEY WOULD BE ABLE TO COMPETE WITHOUT FEDERAL ASSISTANCE, MIGHT DAMAGE RELATIVELY HEALTHY INSTITUTIONS AND REDUCE THE LIKELIHOOD THAT THEY CAN SURVIVE THE CURRENT CRISIS? IN OTHER WORDS, COULD EFFORTS TO PRESERVE THE VAST MAJORITY OF INSTITUTIONS TODAY SERVE TO IMPAIR THE PROSPECTS FOR SURVIVAL OF THE INDUSTRY AS A WHOLE?

3. ON PAGE 7 YOU STATE, "THE BILL PROVIDES MINIMAL REQUIREMENTS FOR THE ELIGIBILITY OF INSTITUTIONS FOR FINANCIAL ASSISTANCE WITH A GREAT DEAL OF DISCRETION LEFT TO THE REGULATORS. .... IN OTHER WORDS, THE BILL PUTS THE FSLIC IN THE POSITION OF DECIDING WHO IS WORTH SAVING AND WHO ISN'T."

DO YOU HAVE ANY PRACTICAL SUGGESTIONS TO OFFER WHICH WOULD PROVIDE OBJECTIVE STANDARDS BY WHICH THE AGENCIES COULD DETERMINE WHO SHOULD RECEIVE ASSISTANCE, OR "WHO IS WORTH SAVING AND WHO ISN'T"?

4. ON PAGE 8 YOU SUGGEST THAT THE 2% NET WORTH TEST IS "UNNECESSARILY RIGID" AND THAT "EARNINGS STABILIZATION PAYMENTS" SHOULD BE EXTENDED "TO OTHERWISE QUALIFIED INSTITUTIONS WHOSE NET WORTH IS DECLINING BUT STILL ABOVE 2%."

WOULD PROSPECTS FOR SUCCESS OF THE PROGRAM BE GREATER IF ATTENTION WERE CONCENTRATED ON SUCH INSTITUTIONS?

WHAT WOULD BE THE EFFECT ON THE COST OF THE PROGRAM IF ASSISTANCE WERE EXTENDED TO INSTITUTIONS ABOVE 2% IN ADDITION TO THOSE BELOW 2% NET WORTH?

5. ON PAGE 5 YOU STATE, "THE ADMINISTRATION AND THE CONGRESS BY THEIR SILENCE ALSO SEEM TO IMPLY THAT THE MERGER SOLUTION IS COST FREE." THEN, ON PAGE 9, IN DISCUSSING H.R. 5568, YOU STATE, "THE INITIAL COST TO THE GOVERNMENT IS CONTROLLABLE AND, IN THE LONG RUN, THE COST WILL BE ZERO."

IT IS HIGHLY DOUBTFUL THAT ANYONE TRULY BELIEVES THAT THE COST OF MERGERS WILL BE ZERO, BUT IT WOULD SEEM TO BE JUST AS UNREALISTIC TO CONTEND THAT THE ULTIMATE COST OF THE CAPITAL INFUSION AND EARNINGS STABILIZATION PAYMENTS WILL BE ZERO. ON PAGE 10 YOU STATE THAT THE "TEMPORARY MORTGAGE WAREHOUSING PLAN," WILL "IN THE LONG RUN, ... INVOLVE NO COST TO THE GOVERNMENT." ASSUMING THAT THE PROGRAM WOULD INDEED BE "TEMPORARY," SHOULD ANY ALLOWANCE BE MADE FOR THE POSSIBILITY THAT SOME INSTITUTIONS WILL BE UNABLE TO REPAY THEIR OBLIGATIONS TO THE TREASURY? SHOULD ANY ALLOWANCE BE MADE FOR THE OPPORTUNITY COST OF FUNDS DEDICATED TO THIS PROGRAM?

HAVE YOU MADE AN OBJECTIVE EFFORT TO CALCULATE WHETHER IT REALLY IS CHEAPER TO PURSUE AN ASSISTANCE PROGRAM THAN TO MERGE THE TROUBLED INSTITUTIONS OUT OF EXISTENCE?

6. ON PAGE 9 YOU OBSERVE THAT THE REQUIRED COMMITMENT TO HOUSING FINANCE UNDER H.R. 5568 "IS WRITTEN FAR TOO NARROWLY" AND THAT "HOME IMPROVEMENT LOANS, LOANS FOR THE REHABILITATION OF OLDER STRUCTURES, AND LOANS FOR MOBILE HOMES" SHOULD ALSO BE ELIGIBLE.

WOULD YOU ALSO FAVOR EXTENDING ELIGIBILITY TO LOANS ON MULTIFAMILY HOUSING PROJECTS?

7. ON PAGE 11 YOU STATE, "WE ARE VERY MUCH AWARE THAT THERE COULDN'T BE A WORSE TIME TO COME HERE AND ASK YOU TO ENACT LEGISLATION WHICH ADDS TO THE OVERALL BUDGET DEFICIT. WE WOULD NOT DO SO IF WE WERE CONVINCED THAT THERE WERE ANY REASONABLE SHORT-TERM ALTERNATIVES. IN OUR JUDGMENT, DOING NOTHING NOW ... RUNS THE RISK OF MUCH MORE EXPENSIVE, LESS CONTROLLABLE COSTS IN THE MONTHS AHEAD."

IS THERE A DANGER THAT ENACTMENT OF A MASSIVE ASSISTANCE PROGRAM FOR THRIFT INSTITUTIONS MIGHT HAVE AN ADVERSE IMPACT ON FINANCIAL MARKETS, ESPECIALLY ON INTEREST RATES, AND THERE FOR EXACERBATE THE PROBLEMS OF THE THRIFT INDUSTRY?

WHAT EVIDENCE CAN YOU OFFER THAT THE PROGRAMS WHICH YOU PROPOSE AND ENDORSE WOULD REALLY BE CHEAPER IN THE LONG RUN THAN A CONTINUED PROGRAM OF ASSISTED MERGERS?

8. CHAIRMAN PRATT HAS TESTIFIED THAT, "WITH REGARD TO THE ASSERTION THAT RESTRUCTURING IS A POSTPONABLE 'LONG-TERM' PROBLEM, WE DO NOT THINK THAT THE CURRENT CRISIS CAN BE DEALT WITH IN ANY MEANINGFUL WAY WITHOUT RESTRUCTURING. THRIFTS' PROBLEMS ARE LARGELY A RESULT OF THE FACT THAT THEY HAVE BEEN CONSTRAINED BY LAW AND REGULATION TO OPERATE IN A MANNER INCONSISTENT WITH THE LOGIC OF THE MARKETPLACE. NO LASTING RECOVERY FROM THEIR PRESENT PROBLEMS CAN OCCUR WITHOUT THOSE CONSTRAINTS BEING LIFTED." (PAGE 15 OF CHAIRMAN PRATT'S STATEMENT.)

WHAT SPECIFIC REFORM MEASURES, IF ANY, WOULD YOU SUGGEST BE INCLUDED IN LEGISLATION TO ASSIST THE THRIFT INDUSTRY, IN ORDER TO ASSURE THAT SUFFICIENT RESTRUCTURING TAKES PLACE TO PROVIDE REASONABLE PROSPECTS FOR LASTING RECOVERY?

9. CHAIRMAN PRATT HAS TESTIFIED, "THAT SMALL COMMERCIAL BANKS, IN STARK CONTRAST TO THRIFTS, WHICH THEY OFTEN STRONGLY RESEMBLE, ARE ABLE TO REMAIN PROFITABLE IN THIS VOLATILE INTEREST RATE ENVIRONMENT IS SOLELY TRACEABLE TO THE MULTIPLICITY OF INVESTMENT OPTIONS OPEN TO THE BANKING INDUSTRY, AND THE ACCESS OF BANKS TO INTEREST-FREE DEMAND DEPOSITS. USE OF EVEN A RELATIVELY MODEST INCREMENT OF COMMERCIAL LELNDING AUTHORITY COULD PROVIDE A SIGNIFIICANT BUFFER AGAINST ADVERSE CHANGES IN THE ECONOMY." (PAGE 14 OF CHAIRMAN PRATT'S STATEMENT.)

WHAT PRIORITY DO YOU ATTACH TO THE ACQUISITION OF COMMERCIAL LENDING POWERS AND TO THE POWER TO ACCEPT DEMAND DEPOSITS FROM COMMERCIAL CUSTOMERS?

WOULD YOU FAVOR AUTHORIZATION FOR SAVINGS AND LOAN ASSOCIATIONS TO OFFER NOW ACCOUNTS TO STATE AND LOCAL GOVERNMENTS, AS PROPOSED BY REP. BILL GRADISON IN H.R. 5414?

National Savings and Loan League

1101 15th Street NW
Washington, DC 20005
202 331-0270 Cable: NATLISA

Jim Cousins
Senior Vice President
For Governmental Affairs

April 19, 1982

Honorable J. William Stanton
Committee on Banking, Finance and
  Urban Affairs
2129 RHOB
Washington, DC 20515

Dear Congressman Stanton:

Enclosed are our responses to the questions submitted on H.R. 5568. If we can be of any further assistance to you or your staff, please call on us at any time.

Sincerely,

Jim Cousins

Jim Cousins

:bc

Enc.

1. If interest rates remain at extremely high levels and if the savings and loan industry is not provided with increased asset powers, our ability to provide housing finance will be limited. The situation today is further complicated by the number of low-yielding mortgages in our portfolios. What we need are the tools to provide additional profit centers in order to keep our net worth at levels that will permit us to continue in mortgage finance. We also need the flexibility to compete with the many non-regulated entities for the savings dollar. In the future, flexible mortgage instruments (which have finally been authorized) will assist us in continuing our mortgage finance role. Interest rates, however, must come down to provide relief to the thrift industry and to allow us to be able to qualify buyers for mortgages when funds are available.

2. We do not believe that the natural selection process can function efficiently in the present environment. The present environment is not normal and its effects do not fall evenly. We would hope that the assistance program could be designed not to save the weakest, but to provide some breathing room for the viable institutions. Massive consolidation through mergers is not necessarily the most efficient method for resolving problems which plague the industry. While some consolidation will be necessary and, perhaps, even desirable, the problems facing the thrift industry go beyond a few weak institutions. The industry, as a whole, is facing its present problems because it did what the government mandated. We believe that the proposed assistance program will provide a more stable environment in which to proceed with restructuring of the industry.

3(b). We would hope that the program will be constructed in such a way as to prevent creation of competitive inequities.

3. No. Today, without the proposed legislation, the FSLIC is essentially deciding these questions. It seems to me that the question of who gets assistance and who doesn't is going to have to be made in a case-by-case manner after review of the individual institution's situation.

4. We believe that there is benefit to be gained by providing assistance to institutions before they reach the critical stage. Such assistance should help institutions who show declining but not critical net worth to stabilize themselves and give them additional time to solve problems.

Obviously, the more institutions who qualify for capital assistance, the more such a program would cost. We might suggest that the Committee settle on a cap for the program in order to control the cost. For example, Chairman St Germain has specified $7.5 billion as an amount for the program.

5. It certainly would be feasible to provide some allowance for the possiblity that some small number of institutions might not be able to repay the assistance. However, if interest rates come down and we return to a more stable economy, we would see no reason why the vast majority of institutions could not return to profitability and repay the assistance.

The current merger policies of the FSLIC and FDIC have been costly. We are concerned about the future ability of the insurance agencies to effect mergers in some cases and about the contingent liabilities being incurred. Any long-term policy which jeopardizes the stability of the insurance funds could have a tremendous cost if public faith in the insurance funds is affected. In addition, if the agencies are not able to effectively continue to merge troubled associations and if public confidence is severely shaken, the repercussions would effect the entire system.

6. Yes.

7. Anything is possible. We do not believe, however, that a limited program would make the current situation any worse for the thrift industry. Housing and the thrift industry have borne the brunt of the efforts to control inflation and to get the economy under control. We simply cannot wait any longer for the program to work if we hope to be around to reap its benefits.

8. We certainly agree that long-term restructuring of the thrift industry is essential if we are to compete effectively in today's and tomorrow's market. Without these changes, the thrifts will continue to suffer these cyclical problems. Specifically, we support the added asset powers contained in H.R. 4724, introduced by Ranking Minority Member Stanton.

9. We believe that commercial lending and commercial checking powers are a high priority for thrift institutions.

Yes, we favor authority to offer NOW accounts to state and local governments.

Both of these powers are necessary if we are to be able to serve the full range of needs in the communities where we are located.

10(a). The FHLBB has been monitoring, on a regular basis, the capital position of all FSLIC-insured institutions. Therefore, this provision is practical and workable. As we indicated in our formal statement, we believe that the Bank Board should have the discretion to use the tools provided by the bill for institutions before they reach the 2% level, providing that other eligibility standards are met. We believe that the Board can, and would by regulation, establish criteria that would protect the legitimate interests of the government and prevent abuses of the program. As a practical matter, we can assume that any institution receiving assistance would continue to be under close supervisory scrutiny until the assistance was repaid.

(b). Given the close supervision we assume for institutions receiving assistance, this provision is workable and practical. Reviewing lending practices is already a normal part of the examination and supervision process. We see no reason, therefore, why this provision should cause any major problems.

(c). As we stated in our testimony, the general purpose of this provision is appropriate but the specifics of the provision are rigid and would not contribute to the overall objectives of the program. As presently drafted, this provision would require institutions to lend new deposits at rates below the cost of those deposits. In so doing, the bill would perpetuate the earnings problems caused by holding below-market loans. In order for this provision to be practical and desirable, the housing investment criteria would have to broaden. Also, the rate should be two percent above the institution's marginal, not average, cost of funds.

(d). Earnings losses would not be subject to manipulation if, as we assume, there are FHLBB regulations and close supervision of assisted institutions. The examination process would easily detect management decisions which might aggravate the institution's losses beyond that attributable to market conditions. We believe that this provision is highly desirable because it can be used by the FHLBB as a positive incentive to cost-cutting and improved efficiency.

FERNAND J. ST GERMAIN, R.I., CHAIRMAN
HENRY S. REUSS, WIS.
HENRY B. GONZALEZ, TEX.
JOSEPH G. MINISH, N.J.
FRANK ANNUNZIO, ILL.
PARREN J. MITCHELL, MD.
WALTER E. FAUNTROY, D.C.
STEPHEN L. NEAL, N.C.
JERRY M. PATTERSON, CALIF.
JAMES J. BLANCHARD, MICH.
CARROLL HUBBARD, JR., KY.
JOHN J. LAFALCE, N.Y.
DAVID W. EVANS, IND.
NORMAN E. D'AMOURS, N.H.
STANLEY N. LUNDINE, N.Y.
MARY ROSE OAKAR, OHIO
JIM MATTOX, TEX.
BRUCE F. VENTO, MINN.
DOUG BARNARD, JR., GA.
ROBERT GARCIA, N.Y.
MIKE LOWRY, WASH.
CHARLES E. SCHUMER, N.Y.
BARNEY FRANK, MASS.
BILL PATMAN, TEX.
WILLIAM J. COYNE, PA.
STENY H. HOYER, MD.

U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
NINETY-SEVENTH CONGRESS
2129 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515

J. WILLIAM STANTON, OHIO
CHALMERS P. WYLIE, OHIO
STEWART B. MCKINNEY, CONN.
GEORGE HANSEN, IDAHO
JIM LEACH, IOWA
THOMAS B. EVANS, JR., DEL.
RON PAUL, TEX.
ED BETHUNE, ARK.
NORMAN D. SHUMWAY, CALIF.
STAN PARRIS, VA.
ED WEBER, OHIO
BILL MCCOLLUM, FLA.
GREGORY W. CARMAN, N.Y.
GEORGE C. WORTLEY, N.Y.
MARGE ROUKEMA, N.J.
BILL LOWERY, CALIF.
JAMES K. COYNE, PA.
DOUGLAS K. BEREUTER, NEBR.
DAVID DREIER, CALIF.
225-4247

April 6, 1982

Mr. Saul Klaman
President
National Association of Mutual Savings Banks
1709 New York Avenue, N. W., Suite 200
Washington, D. C. 20006

Dear Saul:

Your recent testimony on H.R. 5568, the Home Mortgage Capital Stability Act, before the Subcommittee on Housing and Community Development has been received with great interest and studied closely by Minority Members and Committee staff.

Unfortunately, the limited amount of time available at the hearings did not permit as full a discussion of the issues as we would have liked. However, the Minority staff has developed a series of questions designed to give the witnesses a fuller opportunity to present their views for the record.

It would be very helpful, therefore, if you would respond to the attached list of questions. In order to ensure that your answers will be included in the hearing record, they should be received no later than April 16.

Thank you for your cooperation.

Sincerely,

J. William Stanton

JWS:bfd

Attachment

NATIONAL ASSOCIATION OF MUTUAL SAVINGS BANKS

NEW YORK, N.Y. 10166

NAMSB
Since 1920

Cable Address
Savings, New York

WASHINGTON OFFICE
LOUIS H. NEVINS
Senior Vice President and Director

SUITE 200
1709 NEW YORK AVENUE, N.W.
WASHINGTON, D.C. 20006
TEL 202 763-8144

April 16, 1982

The Honorable J. William Stanton
Committee on Banking, Finance and Urban Affairs
2129 Rayburn House Office Building
Washington, D. C. 20515

Dear Mr. Stanton:

In response to your letter of April 6 to Saul Klaman regarding our testimony on H.R. 5568, we are pleased to submit the attached responses to your questions for inclusion in the hearing record. We hope you will find them helpful.

Sincerely yours,

Louis H. Nevins

Enclosure

4/16/82

Response of
National Association of Mutual Savings Banks
to Questions on H.R. 5568

1. Question: On page 3 you state, "Failure to take any action in the present crisis will itself result in a drain on the budget, and may be far more costly in the long-run than a soundly conceived program of direct assistance."

Have you seen what you regard as "a soundly conceived program of direct assistance"? What evidence can you present that such a program would indeed be cheaper than merging the institutions out of existence with federal assistance?

Answer: Our statement regarding the cost of the present regulatory policies was borne out by a recent study by Wharton Econometric Forecasting Associates, a copy of which is enclosed. This study considered a number of alternative proposals for providing assistance to thrift institutions under various economic scenarios. The central conclusions of this study are as follows:

> "A major finding of this study is that under all the economic scenarios...far and away the most expensive way to deal with problem thrifts, short of liquidation, is to force mergers for them. Under our 'most likely' set of assumptions, regulatory mergers for thrifts, absent use of purchase accounting, would cost up to $84 billion over the next three years. If interest rates fall considerably in the next two years, assisted mergers could cost as much as $50.1 billion. Even this lower figure substantially exceeds the expected reserves of the federal deposit insurers. Under the base case assumptions assisted mergers are twice as expensive as the next most costly proposal.
>
> "Mortgage warehousing appears to be the least costly alternative out three years."

As indicated in NAMSB's testimony, we strongly support the thrust and purpose of H.R. 5568. We have also indicated our concerns regarding certain details of the proposal.

We further believe that the program developed jointly by NAMSB and the United States League of Savings Asssociations represents a preferable and ultimately less expensive approach, as compared with the present regulatory policy of forced mergers, in addressing the thrift industry problem. This program has two basic elements: (1) capital infusion and (2) earnings assistance through warehousing of low-yield mortgage loans.

The purpose of the capital infusion plan is to restore and maintain net worth of 1-1/2 per cent of assets through the use of federal guarantees, but without any immediate Treasury outlay. The plan incorporates the instrument used by the Federal Home Loan Bank Board in connection with recent mergers. The mechanism would be an exchange of obligations between the institution and a federal agency. Any institution with net worth below 1-1/2 per cent of assets would be able to issue income capital certificates, which count as net worth, and receive in return a promissory note guaranteed by the federal government. The income capital certificate and federally-guaranteed notes would be retired as the institution is restored to profitability. Only in the event that the institution is liquidated would the federal guarantee be triggered or any outlay by the Treasury be required.

Clearly, the intent is to provide a back-up to the federal deposit insurance funds and to buy time for individual institutions until an improvement in earnings can be effected.

The capital infusion plan is broadly parallel to H.R. 5568, introduced by Chairman Fernand J. St Germain of the House Banking, Finance and Urban Affairs Committee, except that no cash outlays would be required. In this regard, Chairman St Germain has more recently suggested that net worth guarantees, rather than cash, be used to bolster capital positions.

The second element of the NAMSB-U.S. League program would directly address the earnings problem. All depository institutions with at least 20 per cent of their assets in fixed-rate residential mortgages or mortgage-backed securities would be eligible to participate. Eligible depository institutions would exchange at par low-rate mortgages (those with rates below 9 per cent) for variable-rate federal agency debentures indexed to 30-month Treasury yields.

The institution would receive a supplement to its earnings equal to one-half of the difference between the rate on exchanged mortgages and the 30-month Treasury rate. The amount of the earnings supplement, however, would decline as mortgage repayments are used to reduce outstanding debentures. It would decline further if interest rates decline and would be suspended if 30-month Treasury rates drop 10 per cent. After three years, all exchanged mortgages still outstanding would have to be taken back by the institution and all remaining agency debentures would be retired.

Unlike the capital infusion plan, the mortgage exchange program would require budgetary outlays. The cost to the government, however, would be limited to the interest supplement and would be far less than the direct and indirect costs resulting from failure to address the mounting thrift institution problem. The first-year costs are an estimated $7.5 billion. Costs in later years would decline, as noted earlier, as exchanged mortgages are repaid and would be reduced further if interest rates decline.

Variations in the details of the proposals would, of course, alter these costs estimates. Based on the Wharton Study, however, it seems clear that the present forced merger policy would be more expensive.

BEST DOCUMENT AVAILABLE

2. Question: On page 8 you state, "In administering the program, ..., FDIC and FSLIC should be required to use parallel standards so that savings banks and savings and loan associations in similar circumstances will be treated similarly."

Based upon your experience, is it reasonable to expect that the agencies will be able to administer parallel standards? What standards would you suggest be applied?

Answer: The problems faced by savings and loan associations and savings banks have the same root causes: national housing policies which for decades required or encouraged thrift institutions to invest heavily in long-term, fixed-rate mortgages; the failure of federal economic policy to bring interest rates down; and premature deposit deregulation by the Depository Institutions Deregulation Committee. Since the problems are similar, similar solutions are in order. We know of no valid reason why, for example, a savings bank should be merged out of existence if its net worth ratio reaches 1 or 2 per cent, while the same fate might befall a savings and loan association only at zero net worth. It is our impression that differences in the practices of FSLIC and FDIC result partly from differences in the number of institutions that must be addressed and the relative size of the two insurance funds. Another obvious difference is the two Corporations are dealing with very different statutory language. Providing for capital infusion would effectively backstop the two insurance funds and eliminate a major reason for differences in regulatory polices.

A capital infusion program that sets a minimum net worth level, such as 2% of assets for both savings and loan associations and savings banks, should include a provision which would insure that FSLIC and FDIC administer the program in a similar manner in line with the Congressional intent. One way of ensuring this result would be a requirement that capital assistance would be available to any institution unless FDIC or FSLIC obtains a court order showing cause that the institution should be denied capital infusion.

It should also be noted that the House of Representatives has already sought to address the issue of parallel treatment in H.R. 4603. This House-passed measure provides for parity between FSLIC and FDIC in assisting troubled thrift institutions.

3. Question: On page 8 you suggest, "Language should also be added to make unmistakably clear that capital certificates issued by assisted institutions will be treated as net worth for accounting purposes."

What basis does this or any other Congressional Committee have to impose such a judgment upon the independent accounting profession?

Answer: The intent of our recommendation is merely to ensure that a capital infusion program, once it is adopted, be administered in line with the Congressional intent. If the program is to be effective, regulators must treat capital certificates as net worth, eligible to satisfy any regulatory net worth requirement. Such a provision would impose no judgment or requirement on the independent accounting profession.

4. Question: With respect to each of the following provisions of H.R. 5568, please answer the following general questions:

1. How would the provision work in practice?
2. Would you describe the provision as "desirable"?
3. Would you describe the provision as "workable"?
4. What suggestions would you offer to amend the provision?

a. The capital infusion program designed to maintain the net worth of individual institutions at 2%. How many institutions (number and total assets) do you estimate would qualify for the program today? Do you believe the supervisory agencies can determine eligibility with reasonable certainty and fairness? Should limitations be placed upon the prerogatives of management, to ensure that the federal interest is protected and to create a disincentive for institutions to apply for assistance?

b. The reporting and lending practice requirements. What is meant by lending practices? Would the need to administer this provision place an undue burden on the already strained resources of agencies and of depository institutions?

c. The requirement that not less than 50% of annual net new deposits be invested in single-family mortgages for first-time homebuyers who would pay 1% above the institution's cost of funds. Is it anticipated that there will be any "net new deposits" at all? How many individuals would qualify as first-time homebuyers, and how would institution allocate limited funds among numerous applicants?

d. The provision for quarterly "earnings stabilization payments." Is it sound public policy to provide "earnings stabilization" insurance to depository institutions? Are the figures for "earnings losses" subject to undue manipulation by the institutions? How would the agencies determine that payments may continue and make the required certification "that the continued earnings losses involved are caused by general market conditions and not by the actions of such qualified insured institution"?

Answer:

a. Based on the most recently available data, few, if any, savings banks would qualify today. Given present net worth levels and operating loss rates, however, increasing numbers will fall below the 2 per cent level in the period ahead. Assuming continued high interest rates, savings banks representing one-fourth to one-third of savings bank assets will become eligible by the end of 1983. As noted earlier, we strongly support the thrust of H.R. 5568. We believe that supervisory agencies could determine eligibility in an appropriate manner. Similar judgments are being made now in connection with forced mergers.

We see no need for special limitations on management or disincentives, other than those arising from the proposed reporting requirements, the fact that after two years no further assistance will be forthcoming unless the regulators certify that continued earnings losses are due to general market conditions rather than actions of the institutions, and the requirement that assistance must be repaid with interest to the extent of 50 per cent of net income, when net worth reaches 3 per cent or in 5 years, whichever is sooner. Our main recommendation, as indicated in our statement, is that capital assistance be accomplished through federal guarantees and that cash outlays be reserved for earnings assistance. Furthermore, H.R. 5568 already provides that, in order to obtain capital assistance, an institution must demonstrate to the agency a need for such assistance and must have reasonable prospects for long-term viability.

These requirements give the agencies sufficient latitude to protect the federal interest, monitor the performance of management and create disincentives for institutions to apply for assistance.

b. NAMSB would support reasonable reporting requirements in the administration of H.R. 5568. Any burdens that these requirements would place on the agencies and depository institutions are likely to be much less severe than those already being borne as a result of the headlong pace of forced mergers. Capital infusion would slow down the pace of forced mergers and thereby ease burdens on the agencies. The reference in H.R. 5568 to "lending practices" is not further defined. If it intended to prevent unsound lending activity by assisted institutions, NAMSB would have no objection.

c. As long as interest rates remain high, there will be no net new deposits at many eligible institutions. To the extent that there are net new deposits, however, the requirement would tend to perpetuate large-scale low-yield mortgage holdings and earnings losses, which are at the heart of the thrift institution problem. As indicated in our statement, a preferable way of assisting housing would be to provide for a temporary "buy-down" to reduce interest costs to home buyers. This would bring mortgage interest costs within the reach of many home buyers who are now priced out of the market. It would be applicable to both new and existing properties and would maximize the potential for expanding the supply of mortgage funds since all lenders would be eligible, regardless of whether they receive capital assistance.

d. "Earnings stabilization payments" are merely the mechanism through which capital infusion is to be provided. Without such a provision, net worth positions would continue to deteriorate due to earnings losses in a high interest rate climate. The regulators, in our judgment, should have no difficulty preventing manipulation of earnings figures. The required certification necessitates judgments on the part of the regulators. Similar judgments, however, are being made at the present time in connection with forced mergers. In general, all or most of the potential problems of administration cited in this question are already present in aggravated form in the present policy of forced mergers. The regulators must now make judgments regarding management, the accuracy of earnings and other data, the prospects for survival of individual institutions, the policies of institutions operating with assistance, the causes of continued earnings losses and whether these loses are due to general market factors or the actions of individual institutions. Under the present policy, these judgments will be increasingly made "under the gun" as the pace of mergers accelerates. By slowing down forced mergers, a capital infusion program will permit the agencies to make more reasoned judgment regarding all these matters.

FERNAND J. ST GERMAIN, R.I., CHAIRMAN
HENRY S. REUSS, WIS.
HENRY B. GONZALEZ, TEX.
JOSEPH G. MINISH, N.J.
FRANK ANNUNZIO, ILL.
PARREN J. MITCHELL, MD.
WALTER E. FAUNTROY, D.C.
STEPHEN L. NEAL, N.C.
JERRY M. PATTERSON, CALIF.
JAMES J. BLANCHARD, MICH.
CARROLL HUBBARD, JR., KY.
JOHN J. LAFALCE, N.Y.
DAVID W. EVANS, IND.
NORMAN E. D'AMOURS, N.H.
STANLEY N. LUNDINE, N.Y.
MARY ROSE OAKAR, OHIO
JIM MATTOX, TEX.
BRUCE F. VENTO, MINN.
DOUG BARNARD, JR., GA.
ROBERT GARCIA, N.Y.
MIKE LOWRY, WASH.
CHARLES E. SCHUMER, N.Y.
BARNEY FRANK, MASS.
BILL PATMAN, TEX.
WILLIAM J. COYNE, PA.
STENY H. HOYER, MD.

U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
NINETY-SEVENTH CONGRESS
2129 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, D.C. 20515

J. WILLIAM STANTON, OHIO
CHALMERS P. WYLIE, OHIO
STEWART B. McKINNEY, CONN.
GEORGE HANSEN, IDAHO
JIM LEACH, IOWA
THOMAS B. EVANS, JR., DEL.
RON PAUL, TEX.
ED BETHUNE, ARK.
NORMAN D. SHUMWAY, CALIF.
STAN PARRIS, VA.
ED WEBER, OHIO
BILL McCOLLUM, FLA.
GREGORY W. CARMAN, N.Y.
GEORGE C. WORTLEY, N.Y.
MARGE ROUKEMA, N.J.
BILL LOWERY, CALIF.
JAMES K. COYNE, PA.
DOUGLAS K. BEREUTER, NEBR.
DAVID DREIER, CALIF.
225-4247

April 6, 1982

Mr. Arthur Edgeworth
U. S. League of Savings Associations
1709 New York Avenue, N. W., Suite 801
Washington, D. C. 20006

Dear Arthur:

Your recent testimony on H.R. 5568, the Home Mortgage Capital Stability Act, before the Subcommittee on Housing and Community Development has been received with great interest and studied closely by Minority Members and Committee staff.

Unfortunately, the limited amount of time available at the hearings did not permit as full a discussion of the issues as we would have liked. However, the Minority staff has developed a series of questions designed to give the witnesses a fuller opportunity to present their views for the record.

It would be very helpful, therefore, if you would respond to the attached list of questions. In order to ensure that your answers will be included in the hearing record, they should be received no later than April 16.

Thank you for your cooperation.

Sincerely,

J. William Stanton

JWS:bfd

Attachment

Submitted in response to Congressman Stanton's request for additional questions and answers regarding Roy Green's appearance before the House Housing Subcommittee.

Questions for Mr. Green:

1. On page 3 you state that to liquidate as many institutions as you suggest may fail "would cost the Federal Government roughly $90 billion . . . ." On page 11 you state that under the "net worth guarantee program," . . . "a cost to the Government, if any, would arise only in the event of liquidation of the instiution. . . . Though a contingent liability is present, there is no immediate Federal outlay."

Have you made any allowance for the possibility that institutions will not be able to repay the funds or for the opportunity costs involved in advancing the funds, or for the possibility that outlays in future years might be unacceptably high?

1. The possibility clearly exists that some institutions may not be able to repay all of the income capital certificates (ICCs) which they have issued. That contingency is the more likely to arise the higher the average level of interest rates over the coming years. It should be noted, however, that such a contingency as regards ICCs should be compared against the cost of the sliding-scale financial assistance offered by the FSLIC to facilitate merger solutions of problem cases. The ultimate option of merger always remains and, presuming rationality on the part of bidders for weak institutions, assistance for deferred merger solutions will not be more than for immediate action. Only if rates go higher is there any cost in delay.

The general presumption is, however, that rates will trend down. It should be noted that since no real cash resources will initially be involved, the question of opportunity cost does not arise. Conversely, should a payment of real Federal resources eventually be involved for an institution, much the same outlay would have been necessary under a financial assistance agreement. Any approach will involve inordinately high outlays in future years unless rates recede from present levels.

2. On page 7 you state, "The accumulated damage to date demands some assistance mechanisms right now. If they are not forthcoming, housing and the nation will risk the disappearance of a great and dependable mortgage credit resource."

Chairman Pratt has testified that in the third quarter of 1981, the share of mortgage lending accounted for by savings and loan associations was only 8 percent. Given the current net worth and deposit situation in the industry, can you present evidence that the preservation of the troubled institutions will actually affect the aggregate availability of mortgage money in the future? (Page 9 of Chairman Pratt's statement.)

2. Chairman Pratt is correct in citing the downturn in mortgage lending activity during the third quarter of 1981. However, it should be noted that the third quarter was also the

period of the year during which savings and loan associations experienced their most severe outflows of deposits and a dramatic increase in savings costs (thanks to a hike in market rates and the ill-considered decision by the Depository Institutions Dergulation Committee to raise a 12% rate ceiling on 30-month Small Saver Accounts).

Taking a broader perspective . . . the entire year of 1981 . . . the continued commitment of savings and loan associations to residential mortgage finance is readily apparent:

- S&Ls originated $42 billion, or 43% of all long-term mortgages on one- to four-family homes; commercial banks originated 21%;
- S&Ls originated $10.3 billion or 43% of all construction loans on one- to four-family homes; here, commercial bank involvement was greater, 45%;
- S&Ls originated $17.2 billion of all mortgage loans on newly-constructed homes, or 47% of this activity; commercial banks, 17%.

And, savings and loan associations remain committed to housing in the futurre:

- At the end of 1981, S&Ls held $13.3 billion, or 56% of all commitments to make long-term home morgages; commercial banks held 11%;
- And, at the end of last year, S&Ls held $6.0 billion in commitments to make construction loans, or 57%; commercial banks, had 31% of the outstanding commitments for construction loans.

Thus, we repeat the assertion of page 7 of our statement: "Housing and the nation will risk the disappearance of a great and dependable mortgage credit resource" (if S&Ls fail or disappear.)

3. On page 8 you refer to the three-part proposal which the U.S. League and the savings banks have advanced: "Short-term portfolio assistance, short-term capital maintenance, and short-term homebuyer assistance."

Would you provide your cost estimates for each of these programs and your basis for these estimates?

3. The costs of each element of the program can be estimated with varying degrees of accuracy. As noted in answer 1, the ultimate cost of ICCs will depend on interest rates and also on the acquisition of new asset powers to reduce earnings volatility. No significant costs arise in this part of the program beyond those of other solution techniques.

The portfolio assistance element is easily costed. Essentially, all S&Ls and MSBs would qualify under the 20%-of-assets test plus approximately 550 commercial banks. Total loans eligible (coupons under 9%) would be approximately $250 billion. The average rate on these loans is 6%. If the Treasury 30-month rate is 14%, the rate supplement would be 3%, for a total annual cost of $7.5 billion.

The loan buydown cost is equally simple to estimate. A Treasury subsidy of 3% per loan with an appropriations cap of $2.5 billion for the first year would be fully taken down given the strong, underlying demographics and housing demand. Borrower eligibility guidelines would also be necessary to allocate such loans equitably.

4. On page 11 you state, "The first two elements of the assistance package we propose utilize an autonomous Government agency, rather than existing supervisory agencies."

Do you really expect Congress to be receptive to the creation of still another agency to supervise depository institutions?

4. There is little question that the human resources of the Federal Savings and Loan Insurance Corporation

and the Office of Examinations and Supervision of the Federal Home Loan Bank Board are severely taxed today, given the rapid deterioration in the financial health of the savings and loan business. As FHLBB Chairman Pratt and FSLIC Director Beesley have stated repeatedly, their primary responsibility is the stewardship of the FSLIC Fund and its obligation to protect the interests of depositors. Thus, a new Federal program aimed at preserving the institutional framework must be considered an "additional assignment" for an already overworked agency.

We appreciate that the Congress is not anxious to expand the Federal bureaucracy. The agency we recommend might be skeletal in size. Its payroll and expenses would be sustained by subscription fees from participating depositories -- not by the taxpayer. It might resemble a Federal instrumentality like the Government National Mortgage Association -- which operates an extensive secondary market with a handful of employyes. (H.R. 5578 itself appears to call upon the Treasury to establish a subunit to administer a Home Mortgage Capital Stability Fund.)

If the Congress wishes to assign the Administration of capital assistance for thrift institutions to the existing Federal regulatory agencies, we would recommend that clear-cut statutory instructions be provided for the guidance of the regulatory officials in performing this new assignment.

These instructions should assure that institutions which find themselves with deteriorating capital positions because of interest rate trends and market forces -- and through no malfeasance of their own -- are clearly eligible for aid.

5. You go on to point out that "The FSLIC and FDIC's primary orientation is protection of depositors, not preservation of institutions."

Chairman Pratt has testified that, "Should Federal intervention occur, it should be structured in such a way that it is market-disciplined, efficient to administer, and Darwinian in impact, allowing the weakest members of the industry to go out of existence, while preserving the stronger institutions." (Page 16 of Chairman Pratt's statement.)

Chairman Isaac has testified tht, "Our first tenet is that the assistance should be available only on a selective basis. Inept management should not be subsidized with funds intended to provide temporary relief to victims of unexpected and unprecedented economic conditions." (Page 3 of Chairman Isaac's statement.)

Do you believe that it is practical, or desirable, to preserve institutions for their own sake? If they are to be preserved for the sake of housing finance, what evidence is there that their participation will be greater, with a given amount of capital and liquidity in the indstury, with more, rather than with fewer institutions, and that the additional return, if any, is worth the cost to achieve it?

5. While, in isolated cases, the hostile economic environment may have identified and disposed of "the weakest members of the industry", many soundly-managed and community oriented institutions have been victimized by forces beyond their control. The principles espoused by Chairmen Pratt and Isaac have been overwhelmed by a prolonged interest rate seige of extraordinary heights and volatility -- virtually unprecedented in our nation's modern history. In 1981, 329 FSLIC-insured S&Ls disappeared; thus far in 1982, another 102. Many observers are now saying: "we've gone beyond the fat and are now in the muscle."

In pursuit of the Darwinian theory, one practice in particular is objectionable. Candidates for supervisory assistance (as now available) must agree in advance to a merger resolution to be exercised by the regulatory officials when and if they choose a partner. There is little question that such a precondition to assistance is demoralizing to management and may, in fact, be counterproductive as it discourages efforts to arrest financial deterioration of companies.

We remain strong advocates of the unique diversity of the American financial community, with its specialized intermediaries such as savings and loan associations, mortgage bankers, credit unions, insurance companies, brokerage houses, and so forth. Invariably, efforts to simplify the financial structure through amalgamation and consolidation pay some price in terms of hometown and neighborhood service. This is obvious, for example, in the departure of deposits from banks and S&Ls for money market mutual fund investments, and the resulting squeeze on credit availability in towns and communities across America.

6. On page 12 you state that with an expenditure of $7.5 billion, $5 billion of which would be Government funds, it would be possible to "stimulate up to $83.5 billion in home mortgage lending in the coming year . . . ." This ratio of 16:1 would appear to be attractive until compared with ratios achieved by the secondary market instrumentalities. The Federal Home Loan Mortgage Corporation (FHLMC), for example, can finance as much as $50 in mortgages for each dollar of capital.

To what extent do the results which you project depend on use of the secondary market by thrift institutions to generate the liquidity needed to finance new mortgages? Might it make sense, therefore, to use the more efficient secondary market mechanisms directly, rather than through the thrift institutions?

6. Leverage in the marketplace should be viewed differently for market-rate versus subsidized loans. The capitalization of FHLMC is designed to sustain its loan inventory as work-in-progress for its PC program. However, increasing such capitalization and the carrying capacity of FHLMC would not, by itself, stimulate the primary market activity needed for the secondary market to function at higher levels.

To some extent, the secondary market would be needed to supply liquidity for the suggested subsidized loan program.

This need would depend on savings flows (and, thus, on the DIDC) and also on the volume of homes with existing financing which are in the program. The net additional financing is far less for a property on which an existing loan is being repaid.

Access to the secondary market for any housing assistance program must flow through primary lenders unless the Federal Government decides to fund the entire loan rather than a partial rate subsidy.

7. On page 13 you call for "Existing Federal agencies (to) administer the assistance and determine whether an institution demonstrates a need for such assistance and has reasonable prospects for long-term aviability."

How would you expect the agencies to make this determination? Can you suggest an amendment that would provide more objective standards for the agencies to use?

7. This question is apparently taken out of context. The U.S. League does not "call for" the existing agencies to administer the assistance and determine the "reasonable prospects for long-term viability". Rather, we recommend a new skeletal agency (see answer to question #4) and, as noted in a later paragraph, we agree that the determination mentioned is a difficult subjective judgment. We would prefer to see capital assistance available temporarily to cover operating losses at institutions falling below the 2% net worth standard -- to bridge the gap until some economic normalcy can be restored.

An amendment setting forth some direction to the agencies might read as follows:

> "The financial regulatory agencies may refuse to accept the issuance of income capital certificates authorized herein only upon a finding that such issuance, with respect to an individual thrift institution, has been necessitated by factors other than the high level of interest rates. The financial regulatory agencies may require an institution, as a condition of issuing income capital certificates, to agree to reasonable regulatory restrictions on its operations designed to maintain the institution's current financial condition, and which would have material impact on the institution's financial condition; provided, however, that such conditions may not include a requirement that the institution consent, in connection with the issuance of the income capital certificates, to a merger of the institution with another institution."

8. On page 24 you state, "Maintaining capital adequacy is vital, too. . . . . Existing regulatory concepts -- such as the FHLBB's Income Capital Certificates -- may be adapted to sustain capital at some positive level for all thrift institutions."

As you know, the ICC's and the other recent accounting policies of the Bank Board have been highly controversial within the accounting profession. Would the capital infusions to be provided under H.R. 5568 be treated as 'capital' by independent auditors, and what would be the consequences if they were not so treated?

8. The ICC structure was designed as a hybrid security to qualify as equity under Generally-Accepted Accounting Principles. Since H.R. 5568 builds on that foundation no further problems should arise. In general, however, there is no need for perfect conformity between Regulatory Accounting Principles and GAAP. Both systems continually involve bringing their elements closer in some respects and further apart in others. The major

problem is with the publicly-held companies under Securities and Exchange Commission jurisdiction. The SEC does have discretion over the preparation basis for financial statements and, with appropriate disclosure, there should be no insurmountable problem in granting a variance in this instance.

9. On page 14 you recommend that the "Net Worth Guarantee" program be administered without regard to "such subjective eligibility judgments as a determination of 'reasonable prospects for long-term viability'. . ."

Granted, as you say, that "The capricious turns of the interest rate cycles, ... make such long-term assessments very difficult ... if not impossible." What is the justification for investing public funds in institutions which may not be viable in the long run? If the justification is that it would be cheaper to do so than to merge or close the institution, should a specific finding to that effect not be required?

9. We would also note that Chairman Pratt, in his testimony before the Subcommittee on March 24, 1981, similarly questioned the "reasonable prospects for long-run viability" determination:

> Another difficult challenge would be presented by the stipulation in the bill that eligibility for assistance would turn on the Bank Board's determination that an institution has reasonable prospects for long-run viability. A good faith effort to implement such a standard would be extremely difficult. Also, unless judicial review of our determination were rigidly circumscribed or eliminated, we inevitably would be sued by every disappointed applicant, which would tax the resources of our legal staff enormously."

Your concluding question suggesting that the regulators make a specific finding that capital assistance is cheaper than to merge or close an institution is a useful idea to which we have no objection.

10. Chairman Pratt has testified that, "With regard to the assertion that restructuring is a postponable 'long-term' problem, we do not think that the current crisis can be dealt with in any meaningful way without restructuring. Thrifts' problems are largely a result of the fact that they have been constrained by law and regulation to operate in a manner inconsistent with the logic of the marketplace. No lasting recovery from their present problems can occur without those constraints being lifted." (Page 15 of Chairman Pratt's statment.)

What specific reform measures, if any, would you suggest be included in legislation to assist the thrift industry. In order to assure that sufficient restructuring takes palce to provide reasonable prospects for lasting recovery?

10. In view of the rapid deterioration of net worth at our nation's thrift institutions and the urgency of our assistance request, we would recommend that the Subcommittee not risk delay through the addition of specific reform measures to this particular legislation. However, the U.S. League remains fully committed to the broader and more flexible powers contained in Congressman Stanton's bill, H.R. 4724, and similar legislation pending in the Senate. It is important to equip thrift institutions now with broader investment authority and demand deposits so that they might respond in the future to hostile interest rate environments; broader powers could complement the housing credit specialty in which thrift institutions excel, and permit them to maintain lending volume in such periods in the future.

11. Chairman Pratt has testified, "That small commercial banks, in stark contrast to thrifts, which they often strongly resemble, are able to remain profitable in this volatile interest rate environment is solely traceable to the multiplicity of investment options open to the banking industry, and the access of banks to interest-free demand deposits. Use of even a relatively modest increment of commercial lending authority could provide a significant buffer against adverse changes in the economy." (Page 14 of Chairman Pratt's statement.)

What priority do you attach to the acquisition of commercial lending powers and to the power to accept demand deposits from commercial customers?

Would you favor authorization for savings and loan associations to offer NOW accounts to state and local governments, as proposed by Rep. Bill Gradison in H.R. 5414?

11. We agree with Chairman Pratt's observation. To rectify the borrow-short, lend-long mismatch in the structure of thrift institutions and to cope with volatile rate environments, commercial lending and the ability to offer demand deposits deserve a very high priority for statutory approval. Many S&Ls will wish, as well, to expand their real estate finance specialty; thus, removal of certain restrictions found in the Home Owners Loan Act for Federal associations (such as a 20% limitation on non-residential real estate lending) is extremely important, too. In addition to the real estate lending changes called for in H.R. 4724, thrift institutions and commercial banks should be permitted to make direct equity investments in real property to some percentage of assets, such as 10%.

The U.S. League applauds Congressman Gradison and his efforts to win acceptance of H.R. 5414. This legislation would overturn a legal challenge which has prevented the Federal Home Loan Bank Board from allowing savings and loan associations to offer NOW accounts to State and local governments as well as enhance the cash management of public monies. The public funds deposit area has been effectively denied to thrift institutions through the years in many States due to anachronistic collateralization requirements and limitations such as the $100,000 ceiling for Federal account insurance. The arbitrary restriction on NOW accounts is yet another example.

Indeed, if the deposit deregulation is to be handled logically, we see no reason for a continued prohibition against the payment of interest on demand deposits generally, or for a restriction on those eligible to utilize NOW accounts.

12. With respect to each of the following provisions of H.R. 5568, please answer the following general questions:

1. How would the provision work in practice?
2. Would you describe the provision as "desirable"?
3. Woluld you describe the provision as "workable"?
4. What suggestions would you offer to amend that provision?

a. The capital infusion program designed to maintain the net worth of individual institutions at 2%. How many institutions (number and total assets) do you estimate would qualify for the program today? Do you believe the supervisory agencies can determine eligibility with reasonable certainty and fairness? Should limitations be placed upon the prerogatives of management, to ensure that the Federal interest is protected and to create a disincentive for institutions to apply for assistance.

b. The reporting and lending practice requirements. What is meant by lending practices? Would the need to admiister this provision place an undue burden on the already strained resources of agencies and of depository institutions?

c. The requirement that not less than 50% of annual net new deposits be invested in single-family mortgages for first-time homebuyers who would pay 1% above the institution's cost of funds. Is it anticipated that there will be any "net new deposits" at all? How many indviduals would qualify as first-time homebuyers, and how would institutions allocate limited funds among numerous applicants?

d. The provision for quarterly "Earnings Stabilization Payments." Is it sound public policy to provide "Earnings Stabilization" insurance to depository institutions? Are the figures of "Earnings Losses" subject to undue manipulation by the institutions? How would the agencies determine that payments may continue and make the required certification "that the continued earnings losses are caused by general market conditions and not by the actions of such qualified insured institution"?

12. a. Our Research Department estimates that by the end of June this year, 400 institutions . . . representing $95 billion in assets . . . will be at or below the 2% net worth ratio, and thus eligible for assistance under H.R. 5578.

As mentioned in responses to other questions, we recommend that the Congress provide direction to the agencies to assure that institutions may qualify for capital maintenance.

12. b. Unquestionably, supervision of compliance with statutory requirements on lending practices . . . Truth in Lending, Real Estate Settlement Procedures Act, Community Reinvestment Act, Home Mortgage Disclosure Act . . . diverts agency resources from determinations of "safety and soundness". And, under present Fedeal Home Loan Bank Board rules, savings and loan associations provide elaborate data to their regulators on loan applications. Thus, the monitoring of lending practices is a continuing assignment right now. The rigid statutory language of H.R. 5568 might impose some new burdens on institutions -- while contributing very little

information to the supervisory process which is not already known by the regulators -- to the degree that such reports are required less frequently than quarterly or by some different forman than is now used.

12. c. Whether or not there are "net new deposits" depends on a number of factors, including the public's willingness to commit their funds to savings, the level and direction of interest rates, the terms and availability of competing investments, and such Government decisions as the resolve to reduce the Federal deficit and the actions of the Depository Institutions Deregulation Committee.

The audience of first-time homebuyers is similarly imponderable. In a normal year, approximately 20% of the home loans (for both newly-constructed and existing units) go to first-time buyers and approximately 85% of these are within the loan amount limits specified in Section 203(b) of the National Housing Act. Thus it is probably reasonable to assume that 750,000-900,000 potential purchasers might qualify as "first-time" buyers.

Clearly, this would require an allocation mechanism. A fair allocation system would be difficult to construct, since demand for home loans throughout the country bears little or no relationship to the locales where thrift institutions are in need of capital assistance.

Our best recommendation appears on page 15 of our written testimony: "We would prefer to see a housing assistance program open to all lenders, not just an obligation for those in weakened condition."

12. d. It is our understanding that the sponsors of H.R. 5568 no longer intend to pursue direct earnings assistance for thrift institutions but rather to focus on sustaining net worth at a positive level.

As our testimony details, we would prefer to relate earnings assistance to the magnitude of low-yielding long-term mortgage loans in portfolio through a warehousing arrangement. An earnings supplement, funded by appropriations, could be provided equal to half of the difference between the face rate on the low-yielding loans and an index related to current deposit costs, such as the 30-month Treasury rate; the supplement would be suspended when Treasury rates declined to 10%. This temporary "swap" of fixed rate mortgages for variable-rate notes (with the earnings supplement) would be limited to loans (or mortgage backed securities) yielding less than 9% (at the time they were acquired). The program would have a three-year duration.

Such a program would not be susceptible to "undue manipulation by the institutions" and would determine precisely when the agencies would make earnings supplement payments.

Mr. STANTON. My one question would be, Mr. Chairman, in light of the more detailed questions that will be coming, would be maybe a follow up of your remarks, in that as I alluded or interpreted them, it was the general feeling that until we addressed the problem of the older mortgages and portfolios, and can package them in such a way as to rid your institutions of them, in a method in which we can make it saleable, that anything particularly short of that at the moment, would be shortsighted as a means of saving the viability of most of these institutions.

It leads me to ask the question of what you have in this legislation, and I once again commend the chairman for it. Of course, as a tie-in, it is a buy-out of approximately those institutions that reach a certain level of viability, in which, in return for that aid, you would in turn lend out funds to first-time home buyers. Regardless of the rate at which the funds are lent, whether it be at 1 percent, which I do not think that you could do, or 2 percent or 3 percent, it still is a tie-in proposition.

Just quickly, because we do have to move along in these hearings, if you had, considering your own institutions' positions at the moment, and we are looking quickly to the Federal Government for help, what do you think would be the quickest, most effective aid that you could receive from the Federal Government that would help you immediately, regardless of the legislation that is before us?

And Mr. Masterton, would you comment on that?

And let me address one other point. In principle what do you need?

Mr. MASTERTON. The immediate injection of capital is the very first step, Congressman, and I think that the thrust of H.R. 5568 bears that out. It is not, however, a solution to the problem you and Chairman Gonzalez rightly identified. The basic illness is the low-yield mortgage. But if we are not around to deal with the low-yield mortgage, we cannot survive.

There is a basic bit of information that is essential that we have to put up front in this. Let me restate it, it has come out here. There is an assumption by some parties that there is no cost to the current merger route. Well, that is fallacious and the facts are that in the past year, seven mutual savings banks have been supervisorily merged. And the cost on budget, affecting Federal deficit has exceeded $1 billion.

That is "b" as in billion. The figures that the U.S. League has stated that over the next 2 years, that the number of mergers that they are predicting in a moderate interest rate scenario, not low and not high, is between $20 and $45 billion on budget will be expended.

Our figures are that between $5 and $8 billion dollars will be expended in connection with the supervisory mergers in the next 2 years. In short, what we are saying is that the cost is there. We are going to pay as a country one way or another. We can pay now or we can pay later. And we are simply saying that the first step should be the thrust of the H.R. 5568 and once having set that aside, allow us to stabilize the industry for the time being. Let us then get together on the issue, that you so rightly addressed of the low-yield mortgages.

Mr. STANTON. Thank you. Mr. Green.

Mr. GREEN. Congressman Stanton, I wish that there was a one-shot response that would cover the waterfront, but I am sorry to say that there is not.

I do agree with my colleague, Mr. Masterton, that the capital maintenance program is essentially one that would put us in a holding pattern to let us stay with our head above water. The low-yielding loan program is certainly the one that is going to speak directly to the issue that is causing us to be noncompetitive.

But, add to that the buy-down of the interest mortgage program, which would allow us to start generating some lendable funds for providing housing for Americans. It will also help return us to a situation to where we can be viable as an industry once again.

I somehow think that these things go hand in glove with each other, and are equally important, sir.

Mr. STANTON. Thank you. Mr. Muse?

Mr. MUSE. Basically, I agree with that analysis of the situation, that it is a matter of what you do first, I think that what has been suggested is the first step of capital stabilization.

Once that occurs, the other steps follow of necessity.

Mr. COLES. Mr. Stanton, I would like to speak to that personally. I find the idea of receiving direct Federal assistance repugnant and I think that is true of our industry generally. Had we found some other alternatives that would allow us to mitigate the current situation without direct Federal assistance, we would certainly have selected those alternatives.

Therefore, particularly, as Chairman St Germain has, I believe, restructured his proposal, so that there would be no immediate direct cash assistance, we would really support that as the primary and initial way to try to cure our problem.

Mr. STANTON. Thank you, very much, Mr. Chairman.

Chairman GONZALEZ. Thank you. Chairman St Germain?

Mr. ST GERMAIN. Thank you, Mr. Chairman, and thank you, gentlemen.

I certainly appreciate the answers to the question of our distinguished ranking minority member. Certainly that is the reason for my having introduced the legislation and structure it as I did.

A great deal of thought has been given to this. I first convened the regulators, the Federal Reserve Board and representatives of your industries, in October of 1980. And I said to them that we have got to move. Something has to be done. It took until the spring of 1981 for them to come up with a proposal and that proposal was the regulators' bill, which was with the assistance of Mr. Stanton and the other members of this committee, adopted and sent to the Senate last year.

When I met with the Secretary of the Treasury, in February of last year, I stated that there was a very severe problem brewing and it was getting worse with each succeeding day. His answer was that my concern was ill placed and not to worry, as the expression goes, because interest rates would come down.

Well, ladies and gentlemen, interest rates have not come down. We have undergone the most protracted period of high interest rates that anyone of us can remember.

I was still hopeful that we would see some action to take care of the immediate problem that you all face, that the members of your organizations face. It was not forth-coming. And so, we spent about 3 months working on this legislation, beginning before Christmas and right through the recess period, working with the staff on a daily basis.

So a great deal of thought has gone into this legislation. We are still meeting. We had a 3½ hour staff meeting yesterday on further perfection of the legislation. And one of the points that have to be addressed is the U.S. League recommendation to create a separate agency to administer this type of assistance.

Well, I do not think that the trend today is to create a new body. I feel that we do have expertise in the FSLIC and the FDIC and the NCUA and that they can indeed administer the program.

However, I think that it is important that in the legislation itself we be a little more specific as to which institutions would be assisted. It is one thing to say that they must make a finding that the institution is viable and with this assistance it can survive. I am told that there are some who feel that they want a little more specificity.

We will be addressing that. The manner in which the net worth guarantee certificates—I never took an accounting course in my life—but I have been exposed to a lot of balderdash about double entry accounting. My contention is that if the insuring agency under the authorization issues a net worth guarantee certificate that that is just like cash and you do not have to put it on the other side of the book as a liability as well, because if the institution survives, there is no liability. No cash has changed hands.

Flipping back a moment, our new concept would be to authorize and appropriate such sums up to $7.5 billion that would be authorized and the Appropriations Committee would then pass an appropriation setting the guarantee limits. So there would be no outlay, therefore no effect on the budget deficit.

The only time those funds would in actuality be spent would be if the institution were to fail and you would have to ante up the amount of the net worth guarantee.

I am just sharing with you the evolutionary processes that are taking place here. And as I say, we did not contend when we introduced the legislation that it was absolutely perfect, but there had to be a beginning.

Now, I look at the proposal to assist on the low-yield mortgages. Here is the big rub, gentlemen. That is why I say that it would be better to get this first step over with. I am concerned and that is why I am revising the legislation from an appropriation that would be on budget and go to the net worth guarantee route rather than cash. Everybody in this Nation is concerned about the deficit.

When I look at the numbers here and correct me if I am wrong on that 3-year program to assist on those low-yield mortgages, staff tells me that the cost would be approximately $6.875 billion per year for a 3-year period.

Is that close, is that somewhere in the realm of accuracy? Mr. Green?

Mr. **Green**. Mr. Chairman, that would be somewhat accurate, provided interest rates remain at their present level, yes, sir.

Now, of course, if interest rates get down where the administration has been telling us they would for the last 2 years, this thing could self-destruct as it goes down below 10 percent. But you are correct; if they do stay at the present levels, that is the figure that we would be envisioning, yes, sir.

Mr. **St Germain**. Well, Mr. Green, let us not kid each other. Here I was fearful of the $7.5 billion in my legislation over a 3-year period, and boy, look at $6.875 billion a year. Let us be practical. That is a toughie.

Mr. **Green**. Well, Mr. Chairman, I know how much you have thought about this thing, and how much hard work, on the part of the staff and your part has gone into this; but I would like to say to you that this is the basic problem and the basic issue here. It is not a question of whether or not we are going to have expenditures. Because still, the FSLIC and the FDIC are going to be called upon, through deposit insurance, to take care of this through the merger process.

Mr. **St Germain**. Yes, sir. That is one of the big arguments or points that I feel is salient as far as the legislation that I introduced is concerned. I am very, very worried about those costs over and beyond what is in the insuring funds today.

But first things first, I am afraid that we will have to go one step at a time. This is not 3 or 4 years ago. Of course if it was we would not have the high interest rates, you would not have the problem. But these things have merged, they have come together at the wrong time.

So, I think that I am getting my message through. At least I hope I am.

Mr. **Green**. Absolutely.

Mr. **St Germain**. Now, I must say, Mr. Muse, I thank you for the conclusion of your statement and once again, that was very important, to make sure that there be equality of opportunity for all institutions whether big or small. And that we would assist the institutions that are most in need. Certainly we would like to have that number go up to 3 percent, naturally. But again it is a cost factor.

The 2 percent was not arrived at without a lot of gnashing of teeth, believe me. It is there because that is what we felt we could afford and would be saleable to the members of the committee and on the floor of the House and hopefully in the Senate. And hopefully not opposed by the administration.

I thank you for your testimony, and perhaps after the other members have asked their questions, I will have some more comments and some more questions for you gentlemen.

Thank you.

Chairman **Gonzalez**. Thank you, Mr. Chairman. Mr. Carman?

Mr. **Carman**. Thank you, very much, Mr. Chairman and Chairman St Germain. I would like to just comment briefly and compliment you on your general proposals and the tenents you have put forth in this legislation. I am not sure yet that I agree with every part of it, but I certainly think that it shows an awareness of the very serious problem that is affecting not only this industry, called the thrift industry, but the entire financial community.

I think this is much too large a problem to just write off as a one-industry type of a problem. I would like to ask each one of you gentlemen, if some sort of a proposal like this is not worked out and ultimately many of the institutions fail, who will end up owning all of these mortgages at the low interest rates?

Will the Federal Government end up owning these in some shape or form.

Mr. **Green**. Mr. Carman, I am afraid that you have analyzed the situation right. That two things would happen. That we would have an industry that would no longer be viable and that through some form of acquiring those assets through the FSLIC that would be a problem of the Federal Government but I think that superimposed over that sir, is the more important issue that there would be no longer any delivery system in place for the providing of housing for Americans.

And as we turn this Nation from a nation of homeowners into a nation of renters, it is our feeling that we have really destroyed the American way of life and the very fiber that has made this country strong. That would concern me also.

Mr. **Carman**. This may come to you as a shock, but I happen to live on a place called Long Island in the surburbs known as the sterile suburbs, according to one of our local officials up there. [Laughter.]

And down in that big city, the city of New York they had some problem and so forth, as I understand it, and people were not up to snuff and what have you and sometimes what happened was that individuals walked away from houses that they owned.

And low and behold the city of New York came to own a whole lot of that stuff. I was just kind of wondering if the biggest lender in the United States might become directly the U.S. Government, if they had to take over all of these mortgages. And that apparently would be a likely result.

Mr. **Masterton**. Congressman, there is precedent for that, of course, some 50 years ago, and I would hate to think that we were headed again toward that. But I might suggest another little twist to your question if I could give you another perspective to it.

And that is, the method under which we are now merging our institutions requires that our regulatory agencies—the insuring agencies—subsidize the acquiror and what I would suggest is that at this moment in time, where interest rates are so exceedingly high, as high as they have been in the memory of man, that this is the worst possible time for those institutions to be, in essence, liquidating those assets. Because they are marking them down to such a great degree.

But this bill says, let us give it some time, Mr. Chairman, for normalcy, however we define that, to return. Let us not restructure the financial industry, let us not merge at the highest possible cost, let us buy ourselves some time. And those mortgages, which after all, I mean, what is a better security at this moment in history than homes of American citizens.

I mean it is basically at the heart of many of the better things in our society, what could be a better security for us?

But why buy them at a time like this at such a discount?

Mr. **Carman**. I thank you, for your comments on that. And I yield the balance of my time, Mr. Chairman.

Chairman **Gonzalez**. Thank you, very much, Mr. Carman. I might remind the gentlemen, this is precisely what did happen. And HOLC did that pretty much in the 1930's and the government ended up in owning those mortgages and making money. The Government ended up making money on all of that.

Mr. **Carman**. Let me just comment, Mr. Chairman, I think that is great, but from my own point of view, even if they made money, I would just as soon keep them out of that business. And maybe the people that own and hold those mortgages now would be better off holding them.

I read about that stuff, I am not old enough to know about it, but I want you to know that.

Chairman **Gonzalez**. I am. [Laughter.]

Mr. **Carman**. I know. But I would just as soon have the institutions hold onto those mortgages, as opposed to the Federal Government. I do not think that the Government ought to be in that business.

Chairman **Gonzalez**. Well, this is a new point in our Nation's destiny, it is another destiny, another factor, but what I am saying is that we should not be scared away from the concept that has worked. That is the point that I was trying to make.

Mr. Schumer?

Mr. **Schumer**. Thank you, Mr. Chairman.

There are a whole lot of questions that we all have, and I would just like to make one clarifying point, and that is just from my point of view to share with you how diligently I think the chairman of our full committee worked on this bill and how many pressures there are in the other direction. You cannot imagine.

Somebody said if you are drowning, don't ask for a speedboat if a life preserver is being thrown at you. I don't know if that is relevant here, but it is something to think about.

My question, though, is this. I think one of the things that has made this problem more difficult for the nation at large is the fact that there is a feeling that a temporary solution will not be a permanent solution, and that was Mr. Stanton's suggestion and a few others. But if my meager mathematical background is right, it seems to me that what your real problem is, aside from all of the other problems we have in the housing field and everywhere else, which are very important, but the problem is the slope of interest rates as opposed to the level of interest rates.

In other words, if interest rates had been at 15 percent for the last 15 or 20 years, there would not be too much of a problem. The problem is that your income is much less than what you have to pay for money.

It also seems to me that the slope in interest rates has been in one direction, high interest rates have not come down, and the fault for that lies in a lot of places. I put more of it down at 1600 Pennsylvania Avenue than many people might, but the point is, regardless of the blame for high interest rates and apart from all of the other problems we face, if interest rates remain constant although high, and I am not saying they should, but if they do, your problem will decrease over time.

Every year some of those 7 and 5 and 8 percent mortgages are scooped up and you are issuing new ones or other kinds of assets at

15 percent. So the problem turns around at a certain point. I asked some of our New York big mutual banks for some information, and I just received a letter today from one of them as to when that turn-around point might actually occur.

I don't know if you can respond now, but I think that would be extremely helpful, both to solving your predicament and for the committee to know, that this problem will not be with us 10 years from now, one way or another, even if a bill like the chairman's should pass and keep things at an even level for a while.

Do you have any comments on that? I would particularly be interested—well, anybody.

Mr. **Green**. Congressman Schumer, let me say that we would like to respond to that maybe in writing, touching on it more than we could here today, but your question is certainly a valid one.

[In response to the request of Congressman Schumer, the following information was submitted for inclusion in the record by Mr. Green:]

Response Received From Mr. Green

The basic problem in the thrift sector is indeed due to the "slope" of interest rates.

The "slope" of interest rates describes a yield curve plotted from the structure of interest rates for all maturities at a particular point in time.

In normal circumstances money borrowed for longer periods commands a higher price—higher rates—than money borrowed for shorter duration. A graph showing this pattern is said to be "positively" sloped. Starting with shorter maturities on the left, it climbs up and to the right.

The yield curve has been "negatively" sloped for a good part of the last three years; that is, rates on shorter-term maturities have been above longer-term, depicted graphically by a line proceeding downward from left to right.

Accordingly, even on newly-originated long-term mortgages, thrift institutions have been suffering temporary losses, since rates paid to attract short-term deposits are higher than the return available on those mortgage investments.

On a more fundamental level, the slope of the increase in the general level of rates—an upward "ratcheting" of the entire yield curve—has produced a situation where the overall return on the entire mortgage loan portfolio is well below the costs of funds at nearly all thrifts. For the second half of 1981, the Federal Home Loan Bank Board estimates an industry-wide overall cost of funds of 11.27 percent while the portfolio was returning only 10.02 percent.

This negative spread between asset and liability yield structures is completely unprecedented. To operate with this negative spread, institutions must carve into their net worth (reserves).

The steepness of the recent run-up in rates from more normal levels has caused enormous problems. Traditionally, thrifts have managed to work out from under their low-rate loan burden over time by adding brand new loans at higher rates.

As noted, in the current environment, that traditional process has broken down. The negative yield curve has made new loans of only marginal benefit and, since savings flows have been so weak, relatively few new loans have been made.

In addition, the portfolio turnover at thrifts has been exceptionally slow in recent years. High mortgage rates have depressed the housing market with most of the residential activity depending on creative financing and loan assumptions. Thus older loans with low yield stay "on the books". Intervention by State courts to prohibit the exercise of due-on-sale clauses in several jurisdictions has also slowed down loan turnover.

Consequently the average time required to turn over the mortgage loan portfolio has increased from seven years--the rollover estimated in 1979—to fifteen years under current conditions.

Despite this gloomy picture, the problems described above are essentially transitional. Even if rates were to stay at or near current levels indefinitely, the earnings power of thrifts would gradually improve since the low-rate loans do pay off eventually. If the asset structure of the thrift business can be made more flexible by a switch to variable-rate types of loans, this improvement will be accomplished still more quickly. For those institutions with the net worth (reserves) to stay the course, this problem will eventually be surmounted.

Naturally, the transition would be speeded up by any retreat in rates from the current level. Our full statement to the Subcommittee details the number of institutions which will exhaust their net worth in the coming months at various rate levels. Lower interest rates generally will greatly enhance the prospects for a return to normal mortgage lending and community service for many institutions.

The capital maintenance concept embodied in H.R. 5568 has the same effect. It will act as a mechanism to help institutions over the hump as they transform their assets over time. The goal is to prevent institutions which are basically viable from being put permanently out of business through failure to maintain positive net worth during this transition period of negatively-sloped yield curves.

Mr. **Green**. The comment regarding the life preserver, that analogy I think is an excellent one and perfectly describes our situation.

What we are saying, though, is that we are going to be in the water for awhile and that we have got to have some subsistence in the form of food during that time, and that really is our point there.

There is one thing about interest rates that you talked about, low-yielding loans paying off. We went into this situation about 2 years ago where the average life of a long-term loan was somewhere around 8 years, and with interest rates going up as vigorously as they have the last 2 years, people have wanted to maintain those low-yielding mortgages, and so the average life now, according to some of our most recent studies, is maybe 18 years.

Now, further complicating our problem, to get back——

Mr. **Schumer**. But at a higher interest rate.

Mr. **Green**. No, these are still at the low rate.

Mr. **Schumer**. Do you have any comments, Mr. Masterton?

Mr. **Masterton**. Yes. I will try to make it brief, but there are several issues involved. If we had stability, which is the underlying assumption of your argument, we would not have a problem, and if we reach a period of stability, the problems will be ameliorated.

The problem is, however, that change is so discontinuous that we are caught in the midst of it. That is where we are. We have got to see a rollover of our mortgages. That is going to take time They will not roll over unless other mortgages are being made. So housing has got to be active, the economy has got to be active. That is why housing has led us out of recessions before. It makes things happen. And when they happen, it is like the tide that lifts all the boats up in my part of the country. Everyone lifts with it.

So we have got to have that. But if we don't address some other fundamental immediate and long-term problems, we are going to be right back in the same soup again.

First of all, I very much sympathize with Chairman Gonzalez' opening comments about deregulation. We have got to recognize the reality of the problems that deregulation is causing at this minute, not in the long term but right at this minute, of imposing arbitrary short-term deregulation activities that a major sector of the financial industry simply cannot afford now. Not next year, not the year after, but right now.

I could submit an argument and defend it that if we had not had that deregulation over the last 2 or 3 years, many of our discussions today would not be held. I can pose an argument and defend it that deregulation is part of the cause of our problem, but we will not go into the time on that. But if we do not address some other fundamental issues that have been involved in bills in both the Senate and House relative to the long-term balance of powers between our kinds of institutions, the kind of changes, some of which are taking place de facto by mergers, which are happening the Congress addressing it, if we do not address those, if this Congress does not address those and we get through the short-term issue and say it is all over with, Congressman, we will be back into it in the next cycle.

I mean as many laws as you can pass, I would love you to pass one that says abolish interest rates, economic cycles; but that is impossible. We will have another cycle.

Mr. SCHUMER. We will have that bill out next week. [Laughter.]

Mr. MASTERTON. Rest assured we will campaign hard and lobby for it. [Laughter.]

But that is the short term. It is necessary to get through the long term by addressing the issues that the Congressman so rightly puts into his bill, but we have to see all of those pieces come together. There is no quick fix. We know that.

Mr. SCHUMER. I just have another question.

Mr. Coles, did you want to comment?

Mr. COLES. I would simply like to add that what we are addressing is the ability of our associations to create new assets, and if we can determine the rate at which we can create new assets, then we can respond directly to your question, how long will the turnaround time be.

I would only add that another key ingredient in the formation of new assets is that of deposit flows into our institutions, so we are addressing not only——

Mr. SCHUMER. I would just like to see something in writing that takes a macro view as opposed to one individual or two individual banks sending me information on their liability side. I am not going to count them either. I know what is what. But I forget, you guys have strange ways of calling a surplus something that I don't call a surplus at all.

The other question I have is that this afternoon a few people are going to testify, and I just happened to read a statement in which a combination of people said—I cannot find it here—but that the bill before us needs perfecting. I guess we all agree with that. Here it is. But that what they would actually want to see in the bill is—and I will just read you the letter and tell you who signed it, although you can listen to them or your representatives can this afternoon.

It says:

> Specifically, we urge the committee to incorporate into the proposed legislation the guidelines discussed in the joint statement, which follows. First and foremost, these guidelines have a requirement that S&Ls and savings banks advance at least 50 percent of their total assets in long-term mortgages that are either fixed rate mortgages or adjustable rate mortgages with reasonable constraints for rate increases.

I would just like some comments on that.

Mr. GREEN. Congressman Schumer, let me say that our industry wants to maintain its traditional role of being the champion of the homeowner. I think the great majority of our industry recognizes our commitment to housing. Some of the additional activities that we want to involve ourselves in are only for the purpose of better supporting housing over the long pull. The one thing that we have got to keep uppermost in our minds is that there is no way to involve ourselves in the competitive race for savings at volatile money market rates without having an instrument on the other side, the loan side, that flows up and down with the marketplace. You cannot control one of these things and let the other one go free.

We are doomed to failure if that is what we set out on, so this statement has got to be reasonable in that we have got to have income to justify payment of market rates for savings.

Mr. SCHUMER. Is that a consensus, I suppose, among everybody?

Mr. MASTERTON. I think that is very well said. The record shows in States in which savings banks which have some historic difference from savings and loan associations—which you and others would understand from the Northeast—that in those States where broadened powers have existed, the support of housing has continued.

In my own State we have led the country in the breadth of powers for institutions, and we still have between 65 and 75 percent of our assets in all of our banks and housing. We have supported it. We are wedded to it. It is important to us. We just feel that arbitrary restrictions in asset composition is a bad step.

Mr. SCHUMER. There were two parts to this. One was the 50 percent and one was the type of mortgage you ought to hold. What would be your feeling about the 50 percent? Negative?

Mr. MASTERTON. I would just say that arbitrary limits are irrelevant.

Mr. SCHUMER. Any other comments?

Mr. MUSE. My only comment would be this. There is nothing wrong with the 50 percent if you have a viable market condition. No one should be under those sorts of encumbrances to meet some arbitrary guideline if there is no business with those types of products out there to invest in.

The only one thing that comes out of this experience of the last 2 years, that there have been so many changes in the ball game. I am somewhat like the chairman. I have been around a little while. I started in this business, or in the real estate business over 40 years ago, so I did business with the HOLC back in 1940 and 1941. I have been involved in all phases of this activity, rightfully or wrongfully, for 40-some years, so I know something about the commercial banking side.

Normally in the financial community we are not accustomed to making waves. By that I mean we usually move along certain preordained or prescribed patterns. But more things have happened in the last 3 years in the financial community than have happened in the previous 40 years, I believe.

Chairman GONZALEZ. I think the record ought to show that Mr. Muse had reference to chairman No. 1 and not chairman No. 2. [Laughter.]

Well, we will go into round two.

Mr. Stanton.

Mr. STANTON. Mr. Green, I am just getting around to reading your testimony on the warehousing package. This is certainly intriguing. You make the statement that if Treasury rates remain at $7.5 billion, it would require a warehousing of $250 billion in mortages of less than 9 percent. I have checked with the Home Loan Bank Board in the last couple of days, and I am trying to think what they told me. It seemed to me there were about $650 billion all together in institutions's total deposits.

Mr. GREEN. That is in savings and loans; yes, sir, that is correct.

Mr. STANTON. And it seemed to me they gave me the figure of $400 billion of mortgages at 10 percent or less.

Now, they were going to do some checking on that for me, and they were in my office and did not have any statistics. But yours are correct?

Mr. GREEN. Congressman Stanton, I think if you will look to exhibit 4 of our total prepared statement, we have a breakdown, an exact breakdown of the ranges of those loans, and I think that would respond to your question, sir.

Mr. STANTON. All right, I will pass over that one, then. I am delighted to have this material. Like the chairman said, all of us are looking at ideas and suggestions, and of course, we have to base it on the proper figures to work from. Then I once again had to get called out, but I think it was in answer to Mr. Schumer, and rightfully so, you made the comparison between your assets and liabilities where your hand is tied, on the one hand, and your need for an instrument to draw the loans back in, on the other.

I presume you were alluding to some type of a money market certificate that could keep the funds that you now have in competition with your competitors? Did I catch part of that conversation with Mr. Schumer? Was I right in that regard, that you were talking about the deregulation of the asset side and the liability side? Am I right on that conversation?

Mr. GREEN. Yes, sir. You cannot deregulate one side of our business and then require us to invest in fixed-rate, fixed-term mortgages on the other side. We would get ourselves a year or 2 years down the pike into the same problem that we find ourselves in right now. These things must move in synch.

Mr. STANTON. It is a little bit different. I thought maybe you were alluding to the fact of the need for a competitive short-term instrument. There has been talk, and all I know is what I read in the paper, of the Depository Institution's forthcoming decision in the next week in regard to some instrument that would be competitive and the need for that or for 90-day certificates and the rest of the DIDC's agenda.

I guess my question would be this. The problem there lies in will there be a differential or will there not be a differential in that instrument? I assure you I am one Member of Congress that will never talk or never ask a member of the DIDC Committee to sway them in one way or another, and that is because I was naive enough when we set it up to think that what we were doing was removing it from political consideration. That was one of the most naive things we ever did.

But it bothered me and I am sure it bothers other people, too. You know we are looking for solutions to the saving of an industry, and we are very conscientious about it and we are doing it not for the saving of the institutions per se but in the best interest of the United States and our constituents.

But you have to wonder, is this differential an absolute necessity? Is this where your competition comes from? And I am thinking of the smaller banks, more or less, that were in decades gone by, the competitor back home, but in reality now the Sears and Roebucks and the others are going to be the competitors.

Mr. **Green**. Mr. Congressman, we are certainly not suggesting that this differential be a permanent thing. We are on record as saying that we would be perfectly willing to have a differential that would phase itself out of existence as H.R. 4986 phases all interest rate controls out of existence. I refer you to exhibit 1 of our testimony and to that chart. Late 1979 is when the differential was removed. At that time the curve on net savings gained of commercial banks takes a remarkable, steep rise. At that same time the slope on inflows to savings and loan associations and thrift institutions starts dramatically downward. It continues dramatically downward.

During the same period of time, profits at commercial banks take a rise, and profits at savings and loans just continue to deteriorate. We are saying that one element of solving this problem on a short-range basis could be the return of a differential on a short-term account, and that that would speak to our problem of liquidity, having funds available. It would be something that would not cost the Federal Government 1 cent to assist us in.

Mr. **Stanton**. Thank you, Mr. Chairman.

Chairman **Gonzalez**. Thank you, Mr. Stanton.

Mr. Chairman.

Mr. **St Germain**. Thank you In response to one of Mr. Schumer's questions I think one of you answered that deregulation, the actions of the depository institution's deregulatory committee, has been very harmful and deleterious to you in increasing the rates that are paid on most small savers certificates, et cetera, et cetera. Did I hear correctly?

Mr. **Masterton**. I believe that was my comment, Congressman.

Mr. **St Germain**. By the same token, were you still under the previous constraints, a lot of this could have happened anyway, and I think it would have had to happen anyway. You cannot ignore what Mr. Stanton brought out; you cannot ignore the money market funds. I mean they came into play, again an accident of circumstance, but they really took off, so to speak, about the same time as this occurred. Absent the certificates, the higher yielding certificates that you have, I feel very strongly it would have been a total disaster because the money market funds would just have eaten it all up.

Am I not accurate in that?

Mr. **Masterton**. Well, we certainly concur with your statement about the money market funds, Congressman. We remain very concerned about their role. They have been the great cause of our deposit outflows. We can easily trace them, readily trace them. Our concern remains that they are under so few of the restrictions that we are under, for example, the absence of reserves on what have obviously become transaction-type accounts. Without those obligations they have just continued to grow, and you are certainly right, they are consuming great dollars, billions of dollars of our moneys. There is no question about it.

Mr. **St Germain**. Your are from the State of Maine.

Mr. **Masterton**. Yes, I am.

Mr. **St Germain**. We had hearings back, I think, in 1978, at which time, having done a study, we found that some of the commercials up there were still paying 3 percent on their passbook accounts. Do you know what the rates are now on passbook accounts?

Mr. **Masterton**. Well, I think that they may still be under 5 percent in some cases where there is little competition. In 1975 we got statewide branching laws passed, and I think that generally competition has brought them up. But we have not been immune to the money market funds in our area. We can trace a study done 2 years ago. At that point in time over $200 million of funds had flown out of our State, and as we have testified many times, I know of no money market fund that has ever made a home mortage loan or an auto loan or a construction loan or helped any of us redevelop our cities, and that burden has remained on us.

I can tell you in our State and throughout New England, as you know, Congressman, the role of our thrift institutions, redeveloping our cities, whether it is Providence or Bridgeport or Portland or Boston, those roles have been significant. And we cannot now simply say, well, the Federal policy has changed, we are now going to bring down inflation with high interest rates, your 40 years of supporting urban redevelopment and housing were fine and thank you very much, but now we are going to find someone to merge you with out of Los Angeles or Chicago.

Who is going to take over that task? We talk about a 50-percent responsibility for housing. I have 25 percent of my resources in commercial loans, a quarter of which are in health care. Who is going to take that over? No doctors offices, nursing homes, hospitals from one end of my State to the other.

The essential problem that the Congressman addresses in the bill of buying us some time to deal with the fundamental issues is the first order of priority again, Congressman Stanton. Without capital, you do not exist. You become illiquid. And that whole confidence, not only the accounting technology of it but the public confidence, has just got to be restored now.

Mr. **St Germain**. I do not know if you gentlemen are aware of this. Do I recognize Mr. Wolfe?

Mr. **Green**. Mr. Wolfe had to leave. He had an urgent situation he had to go to. Sir, this is Mr. George Briody from the Chicago area, and Chicago, as you know, is one of the hardest hit areas of our country in the business. He was in charge of our capital maintenance program committee, and if you have the time, he would like very much to at least make a very short statement.

Mr. **St Germain**. I am sorry Mr. Wolfe left because this committee went to Seattle, Wash., for a hearing on the economy, and we encountered a most unusual situation. We saw a picket line out there, the best-dressed pickets I have ever seen in my life, led by Mr. Wolfe. They had all of these S. & L. and mutual people picketing. They were a little upset with a fellow named Paul Volcker, and they had this sign. It was a regular, good old-fashioned picket line with about 200 of them circling the entrance.

Mr. GREEN. Mr. Wolfe also, Mr. Chairman, is the one who drove his Model T or Model A from Spokane to Washington, D.C., with the door of his safe, saying that you have taken everything else away from us, here is the door to the safe, too.

Do you have time for a comment, Mr. Chairman?

Mr. ST GERMAIN. Well, before that, I just want to make this observation. Yesterday we had the homebuilders and the realtors and the mortgage bankers testifying. Now, you people have got a problem. They are upset with you. Are you aware of that?

Mr. GREEN. I understand there are some differences of opinion there.

Mr. ST GERMAIN. I tell you, they didn't equivocate. So I think you had better engage in a discourse and have communications with them because in the past you have worked together on behalf of the home purchasers. I think it was a good working relationship that you had and I am hopeful that you can reestablish that in the near future for the benefit, frankly, not of yourselves and not of the homebuilders and the realtors, but for the benefit of the people out there that would like to be able to buy a home and for the people who are out of work because the saw mills have shut down in Seattle and there is no work for the people out there felling the timber.

The carpet manufacturing plants in the Atlanta area are shut down. The hardwood plants that supply the furniture industry are just about out of business as well. They are not doing a darn thing. There are a lot of people out of work as a result of that. So it is important, I think, to our economy and to the home purchasers and to the people that work in homebuilding and all of its satellite industries that you have a meeting of the minds and get together again.

Mr. GREEN. Certainly your advice is extremely good, Mr. Chairman, and we will continue to try to do so; but we have found that the survival instinct is a very strong one, and this is really what we are talking about here today, sir.

Chairman GONZALEZ. Mr. Briody, would you like to make a statement?

Mr. BRIODY. Thank you. I think Roy Green asked for me to speak just to dispel the notion that I came here as his bodyguard. [General laughter.]

I am from Chicago. In our area, there is only one major institution given current circumstances that has enough net worth to be around at the end of next year, and I am talking about the major institutions, the large ones. I am a little institution. So I compliment you, gentlemen. You are right on target with an awareness of what the problem is, and Chairman St Germain, you echoed my sentiments exactly when you said these asset expansion powers are nice, but unless we do something today we are not going to be around to enjoy them, and I think that is about the situation that has been pretty well stated up and down the witness table here.

Chairman GONZALEZ. Thank you very much. I wanted to say I did not get to meet Mr. Wolfe, and I was not able to join you, Mr. Chairman, unfortunately, on that trip to Washington, but had I known of this, I certainly would like to have seen him, to see how he could help me rustle up some support for my impeachment resolution of Paul Volcker; but we will just have to find a way to contact him later to see what kind of influence he can muscle up for me here in the Congress.

The only reason that I am going to indulge and impose upon you is to continue some of the very important, I think, the critical things. I might also add, Mr. Chairman, you mentioned about the homebuilders and all. The impression I had was that they were not so much put out with the savings institutions as they were saying that they felt the savings institutions had been compelled to convert into banking, to go into the banking business, and therefore they echoed what I have been troubled with, and that is that this problem that confronts us today is radically different from what we have had before, even if interest rates were to fall, and part of it has been the congressional action on such things as deregulation and the like, in which the structural format has been changed.

There, I would like to emphasize two parts of Mr. Coles' testimony, because I think in my opinion he hit the target on page 2, where he says, since the early 1930's there has been a well-understood policy of the Federal Government to assume substantial responsibility for the stability of the Nation's financial intermediary system, which ipso facto provides also the credit resources for home construction, and this is what we have said repeatedly in introducing the 1982 Housing and Urban Development Act.

The other was a complementary statement to that thought on page 4, at the beginning of the second paragraph, and I quote:

> Beginning about 4 years ago, the market and the Congress told us we were not paying a fair rate of return to our depositors. As a result market sensitive instruments were created to stem this disintermediation, and give the saver a fair shake.

I think those two salient points are the things that we basically must address fundamentally, even though in the meanwhile we have got to praise the chairman and thank him for doing what has to be done now, at least insofar as one immediate step of attempting to save the day.

This leads to the fundamental question I was going to submit in writing, and that is that though the purpose of the bill which we have appended to this hearing is to preserve the mortgage lending industry, there are many among the homebuilders and others who contend that mortgage lending is what got us in trouble in the first place, if the industries to be saved, either through this bill or some other mechanism, will continue to make the lion's share of mortgages, or will it be compelled to move aggressively into other areas for its own self-preservation, that is, competing with the banks, competing with the new gimmicks and all, and this is a fundamental question, and we are going to have to address it, as I see it, Mr. Chairman, inescapably, and perhaps as soon as possible.

Do you feel that even, say, if interest rates were to fall and dramatically, I mean, really dramatically, say by the end of this month, down to 12 percent or less, even, would that in effect insure the return of the savings institution into the fixed long-term mortgage activity?

Mr. COLES. If I may.

Chairman **Gonzalez**. Yes, Mr. Coles.

Mr. **Coles**. I know that some of our sister organizations in allied industries are concerned that we as institutions will become banks, and if a bank is defined as a financial intermediary who tries to strike a balance between its assets and liabilities, yes, we will all become banks, because that is the only way we can survive.

Chairman **Gonzalez**. You have to do that now.

Mr. **Coles**. We have to do that now. But then, there is a large and rapid jump to another conclusion that if we are banks in this balancing of our assets and liabilities, we then change the orientation of our lending, and that, sir, I believe, is not necessary.

For example, in our State of Texas, we have for the last 15 months originated all of our loans on the basis that the rate is adjustable in accordance with our State law, and on that basis we were able to be profitable on a marginal basis, even during an environment of very high interest rates, and there are a number of mortgage instruments that, although the interest rate risk is shared between the lender and borrower, also provide for payment plans that will enable first-time homebuyers and upgrading home buyers to continue to obtain the kind of housing that they seek.

So, there is no question in my own mind that with the new powers we have on the asset side in the mortgage field, in the real estate-related field, that we will remain primarily, overwhelmingly in the mortgage field.

Mr. **Green**. Let me just add to that, Mr. Chairman, that if our industry had the feeling that interest rates were down, and would have some degree of stability, I think you would see a lot of people offering fixed-rate, fixed-term mortgages. However, I think the average thrift industry executive has some great concerns over whether or not we are going to have that stability, and we have got to protect ourselves.

You know, we hear a lot of talk about the problems that the consumers see with the adjustable rate mortgage. Let me just submit to you, sir, that if we had been given 15 years ago the adjustable rate mortgage that we really said during that time was important to our longterm well-being, that in this highest interest rate period in history now, that we could be loaning money out on an ARM at 13½ percent and still be making money, because of the average portfolio rates of our loan portfolio at that time. So adjustable rate mortgages with consumer safeguards, which I think the marketplace will absolutely dictate, could be very much in the best interest of the citizens of America.

Mr. **Masterton**. Mr. Chairman, I would add a few things to that. I think that it is our belief that embodied in the savings banks and savings and loans of America is the greatest mortgage originating and servicing capacity known in the world's history. That capacity can be used and is being used to originate loans for sale to other investment markets. So, it is essential that we see the chain from production and sale to origination and service to eventual ownership.

Now, if we are selling those loans, and in response directly to your question of will we make long-term fixed rate loans, I would return to you another question: If we are originating them for sale, who is buying them? Are the pension funds going to buy fixed rate loans? I doubt that. Now, perhaps, if they can see a non-variable rate to their pensioners, maybe they will. Will the public accept a fixed rate of return on their monthly benefit? The answer is no. Therefore, the question, can they make investments that have a fixed return, and the answer again is, I doubt it.

Will FNMA take solely fixed rate loans? Well, many will contend FNMA has enormous difficulties that are now caused by their fixed-rate loans, and intended well-being provisions of assumption.

So, if you look at models, as many of us have in Great Britain and the Scandinavian countries, where they continue to make loans, those loans are made for sale to secondary markets. They are often pegged right to the cost of their certificate, and all float within the same cycle, and the business continues.

My guess is, our guess is, that the fixed-rate, long-term loan may no longer exist in the financial world. So, the question of whether we originate it may not be the germane question. I think what we will see as we develop in the future, again, leaning on the comments that Mr. Green has made, that our need to develop variability in our earnings as our primary competitors—the money market funds and the commercial banks have—will be essential. You have to have equal earning capacity to pay equal rates.

So, I think that is the fundamental direction we must go to. I understand the irritation that the home builders and realtors have with this, and my only response is, if we are not here, how can we help you? We have to be here at some level to help you. It may not be 100 percent of our resources, but they have always had our commitment to work with that area. They have got to trust our commitment in the future.

Chairman GONZALEZ. That is very true, sir, and it is the issue, but no nation, unless committed, and providing a mechanism for such things as mortgages, for the purpose of home construction, has ever developed, and you have to have a mechanism. As Mr. Coles pointed out, since the thirties, we have had it, and it has been mostly in this institutional activity. Now it looks as if we are faced with the dilemma that you so eloquently described, Mr. Masterton. I do not agree with the fact that high interest rates can be lived with.

All the history, throughout the written history, on interest rates—there has been, at least as of about 3 or 4 years ago—a book written by a very diligent man who has for years lived in the New York Wall Street area, and he wrote a book, "The History of Interest Rates," and it is very dramatic in what it documents. It is a very expensive book, let me warn you. I had to pay $40 for it.

But what I am trying to say is that if the thought is that a Nation such as this, with its economy structured such as it has been and is, and the basis for what we call the American way of life, thinks that it can live with usurious and extortionate rates of interest, it is making a fundamental and abysmal error. It is deluding itself. No nation in the history of mankind's development—this is the reason why, even in the time of Jesus Christ, it was against the law to charge one-tenth the rate that has been legitimatized on the national level.

The idea that in a country such as ours, we would have interest rates of 21 percent, is just impossible to believe. Those of us that have a little bit of background that exposes us to other countries, we call that the Third World or undeveloped country type of economy, not in this mass production, mass consumption, mass credit availability, installment purchases, and the like, which is the basic, and when we come in with these extortionate rates of interest, and the Congress sits by, and we suffer the reenactment of the same conditions that led even to the Depression of 1907, that in turn led to the enactment of the 1913 Federal Reserve Act, and then to sit here, Presidents, leaders of Congress, the Chairman of the Federal Reserve, to try to tell us that interest rates are an act of God, there is nothing that can be done about it, is just absolutely unacceptable to me.

Maybe I am radical on that, but I have not yet seen any reason why on an intelligent, rational basis I can accept that argument, and I have seen industrial leaders, and I have seen financial leaders accept it and act as if this is an act of God, and yet I think it is at the basis, at the root of the whole problem. I don't care what anybody says. And unless and until we do that, this country is going to be pilloried. It is going to be crucified on this cross of extortionate and usurious interest rates, and that is exactly what we have.

We have legitimized usury, and I say to you, gentlemen, that we can have all of these gimmicks and everything, but until we get some control over that, and it is controllable, I keep asking the economists and the chairman, why is it? They talk about deficits and inflation. Well, at the height of World War II, 1945, you look at the statistics. We were utilizing 46 percent of the total gross national product on the Federal level, and yet the Government never had to pay even on an average of 2-percent interest. Truman, the same way, conducted a war.

Now, granted, there were things that were done. There was taxation. There were other things. But what I am saying is that you had worse inflationary factors potentially there, far more destructive, potentially destructive, than what we say we have had since 1971, when the Congress, in extremis, adopted the so-called Economic Stabilization Act.

What I am saying, gentlemen, is that we have got to address ourselves to these equally fundamental issues that are, I think, at the bottom root cause, and in the meanwhile, of course, we can and we should. I think that you have realized that on this level, on the representative level. There is and has been deep concern that we have not accepted Secretary Regan's callous remarks, headlined in the Texas papers a little less than 1 year ago, with respect to the failure of, I think it was a Chicago savings and loan, which was the first recorded type of defunct activity since the Depression, and his idea was that there is no Federal responsibility, and don't look to the Federal Government.

What I am saying is that on the representative level, on the congressional level, there is this bill that the chairman and the others that support it, are bringing forth as an attempt to recognize not only the imminency of the problem but the urgency for action on our level.

Mr. STANTON. Mr. Chairman, will you yield?

Chairman GONZALEZ. Certainly.

Mr. STANTON. Thank you very much, Mr. Chairman. I certainly would not let your remarks pass without stating for the record that if the Honorable Wright Patman were still with us today, he certainly would agree with you.

Mr. Green, since we are taking the time here to give our thoughts on this extremely important question, I have two questions in principle. The one approach, of course, is to help failing institutions with capital infusions or whatever you would want. By doing that, of course, you automatically help some institutions and you don't help others. You create in the marketplace to a degree some day a competitive advantage for institutions that have received Federal help.

That could occur as a result of targeting people who are a certain percentage or ratio of assets to liabilities below a given level of net worth. Of course, your swap program would apply, as I understand it, to all institutions. Am I correct? All savings institutions, primarily; maybe some small commercial banks? I understand, under your guidelines, only 15 of the 2,000 credit unions would be involved.

Some of us on the committee, like the chairman and I, of course, have been through New York City, and some certain parallels can be given, Chrysler Corp., and in all of those cases, the restrictions that were imposed by the lawmakers upon the institutions in the city receiving aid were very stringent, very, very tough. Many people think we not only bailed out New York City, but in the final program that was put together by President Ford, no other city I know of came forth to ask for the same kind of treatment. That was very tough.

I think the other automakers would agree with Chrysler. I mean, the Federal Government is involved in the day-to-day operation, that the people assigned by the Treasury Department have moved into that corporation.

In all of this talk on savings and loans, I have never heard of there being any restrictions or requirements in regard to these institutions that would receive Federal aid.

Would you have any thoughts in regard to that? Do you think that that is a fair question to ask, and that we should explore that when aid is given, depending, of course, upon the type of aid, that certain restrictions attach to it?

We are coming around to at least talking of something, you see, and when you go afoul of that, you do think out loud, maybe, of the problems that one foresees down the road with our colleagues or ourselves. You obviously, in the cases where you do help everybody, or where you are helping some and you do not help others, have to consider improving conditions. We know we are going to help some people that are going to go regardless, and should we give thought to the types of restrictions that people should receive? Why should we give it to your organization and then allow you to go out and get a 25-percent salary increase?

Mr. GREEN. Well, Congressman Stanton, let me say that the capital maintenance program—we have some examples of this on a preliminary basis—that the Bank Board has already used. There are some stringent requirements that go along with this; I think as a general rule our industry and our institutions would not particularly like to have a Big Brother there with them.

However, if this cannot be avoided, here again, self-preservation is of the utmost importance to us. All institutions, whether they were above this arbitrary percentage net worth requirement, would have the benefit of having the safety net if things continued to go in the direction they are going. And so, this would be something that could be beneficial to all institutions over the long pull.

You are right that as we envision the swap program, all types of institutions, I think, if they have a certain percentage of loans within their portfolio that are long-term residential type loans, would qualify.

The only other comment that I would like to make is that there is a difference between the thing that you have described, and Chrysler: Basically we have a partnership that we have had with the Government, a partnership not only in the insurance of accounts, but in the delivery of loan services to Americans to provide for homeownership. That partnership that has sort of channeled us into the position we find ourselves in now, we think, is a very logical and good reason that the Government, too, should be a partner with us in a short-term situation to allow us to essentially come through this period to where we can return to profitability and return to that mission of providing for the legitimate borrowing needs of households of Americans once again.

Mr. STANTON. Mr. Green, though, if you follow your logic to the proper conclusion, couldn't you reverse that and almost say that we have a partnership, and therefore the Federal Government is entitled to make sure you have a profit? Do you think that is the case?

Mr. GREEN. No, sir, I don't. I guess one could argue that, but I certainly would not look for that at all. We have just changed essentially the rules of the game here, in that through 30 or 40 years of saying that you have got to do a certain thing because there are national housing goals that this country feels are important, and that the only instrument that we had available for that purpose until May of 1981 was the long-term, fixed-rate, fixed-term mortgage, all we are saying is that that is a problem that we would like for you to help us speak to on a temporary basis.

Mr. MASTERTON. Mr. Chairman, I would add one small item. I think that Mr. Green has evidenced a difference between the types of situations, New York, Chrysler, and so forth, that you describe, not only the difference that we start out with the Government having a contingent liability that did not exist there, but also the fact is that we already have in place regulators who set those kinds of stringent requirements.

We have suggested, and I can understand the reasons for your criticizing a new agency to really operate between and jointly with FDIC and FSLIC. The reason is that currently both of those insuring agencies use different standards in dealing with, for example, net worth requirements. A savings and loan can operate to zero net worth, and continue to be allowed to operate, whereas the FDIC really gets pretty apoplectic when you are 3½-percent net worth. The FDIC has a minimum of 5-percent net worth standard while the FSLIC is 3 percent.

What we are suggesting is that there be some evenhandedness here, and an agency which really could be staffed by the combined group should be charged with what we would suggest is the broad discretion in flushing out the intent of the Congress, setting out those particulars that would be consistent between the two, but be very specific as to your expectations.

That is the principal reason why we suggested another agency between the two existing ones, and we are suggesting that it should be no cost, if possible, a board perhaps that even not only has both agencies represented but perhaps the industry itself, and also the State examiners who have a major role in this. They are very often being preempted on a State level by Federal action, and their voice should be heard as to the intent of the thrust. That is the way we see that policy board that could follow through your intent, Congressman.

Mr. **Stanton**. I don't know whether or not you need another agency, another board down the road. Certainly, the combination of the existing two boards into one head—I can foresee that—and I can foresee, in a historic time in the period that we are in, of the need for Government understanding of a transitory period, the type of which we have not had in 50 years.

I think as we look down the road 10 or 20 years now, with all of the changes and everything, it is certainly conceivable that the institutions as we now know them, or their assigned responsibilities, will no longer be there. It is getting through this transition period in which you have to read twice some of these suggestions that are given on how to handle, in a free situation, some of the transitory situations in which these institutions find themselves.

It is going to take a lot of leadership. It is going to take a lot of understanding, and it is going to take some changes in traditional thought among the political parties to face this, because it is just going to change, and it is going to change whether we want to have anything to do with it or not. I think the money market certificates are just the tip of the iceberg, I really do, of the changes that are coming.

Mr. **Masterton**. Congressman, with the thrust of this bill, I hope we will be around to help participate in that change.

Mr. **Stanton**. Well, I appreciate that, and I hope so, too.

Mr. **Coles**. Mr. Chairman, I would just like to respond to a portion of Mr. Stanton's comments, and I hope that in H.R. 5568 there will be a mechanism that allows the continued consolidation in our industry, and that those inefficient operators can be combined with other institutions to make not only stronger individual units but a stronger industry. I think we would not attempt to mislead you and say that although we have been a sheltered or protected industry, we do not have any inefficient operators.

If this is going to keep alive all of the inefficient operations, we would not be supportive of that concept.

Mr. **Stanton**. Mr. Coles, I am sure I am reading the chairman's mind here. Where have you been? Our regulators bill on which we spent so much time and effort to try to lay the groundwork and to fashion an orderly transition of interstate type of institutions, it got so shot down by, regrettably, some of the institutions that are sitting at this table, that it has kept the other body from acting. But those fundamental changes have to take place.

You have got to forget about some old positions when you get into the subject matter we are into now, it seems to me, anyhow; I mean, then we have to expose and explore the whole realm of regulation, and the differential, and all of the other stuff that takes place. Otherwise, you are going to fall farther and farther and farther behind. It is criminal that we didn't have that regulators bill 3 years ago.

Arthur Burns first talked to the chairman and me about that bill, and all of this time could have been saved, and many of these problems could have been avoided, and we just would have been so much better off, but we do not want to make the same mistake today. We do not want to make the mistake of acting in haste, without some kind of a follow-through or follow-up program, so that what we do is in the best interest of the majority of the depositors of our country in the long run.

Mr. GREEN. Mr. Stanton, as to Mr. Coles' comments regarding inefficient operations, let me say that intellectually I agree with that 100 percent. I do hope that this committee understands that when you have got a portfolio that because of public policy yields 11½ percent, and you have got a cost of money of 13½ percent, you can be a brilliant manager who has served your community well for 30, 40 years, and not make a profit.

And because in certain areas of the United States that have had very flexible laws regarding the use of other investment authority, variable rate mortgages of some type, that those, because of geographical locations, are able to withstand the ups and downs of the interest rate market more than others. That is no reason to just assume that because some institutions are in a loss situation, that mismanagement has gotten them there. The chairman's comments about the real core of the problem is interest rates that are absolutely deplorable in this country; that is the basic issue there.

Mr. STANTON. I do not think it is, Mr. Green. I think that the basic issue is competition, and to a degree, we are following in the same pattern now as perhaps we did before. The Government did not insist on regulation Q or on ceilings, rate ceilings. The industry came to us, as I seem to surmise. It was not the Government that solely, alone—we would have been receptive to other ideas of the different types of portfolios along the way if they had come about.

I am not sure about that, because maybe we would have been locked in, too. But it is a combination of many factors. I will say that.

Chairman GONZALEZ. Let me say that it is true about competition, but that is exactly the point. When freedom for the pike means death for the minnow, and the whole idea of our governmental regulatory concept has been to give some chance of life on an equal competitive basis, not to eliminate competition.

But let me also say for the record and then try to wind it up, that the so-called bailout, I have always resented that word because the Government did not give anything in Chrysler's case. Chrysler has since been able to pay the Government $1.2 billion in taxes, just since the so-called loan guarantee. And why? Because the banks would not give a line of credit, even at 15 percent, unless we had the Government's guarantee.

That is how much faith the bankers had in free enterprise. And Chrysler also has since come up from number four to number one, if you talk about competition. But the Government had not given anything. In fact, Chrysler, as I say and repeat, has paid $1.2 or 3 billion in taxes to the U.S. Government because it was able to stay alive and it could get that line of credit on the basis of a guarantee.

And so, it wasn't a bail-out in the sense that the Government was coming in to give it anything; it was guaranteeing, taking that risk on the basis that the managerial know-how was there, even though the critics and the opponents here in the Congress have now said that that was the main reason why Chrysler was in such trouble. That they had not desisted in producing the gas-guzzlers and the fancy fine cars and all that.

But these were the charges that we were hearing in the Congress, and I am thankful that Congress went along—and I was one of those that voted for it—but I do want to say that I do not look upon this as a bail-out of the S. & L.'s or the savings industry. And it is absolutely true, as I pointed out in Mr. Cole's statement, that this Government has had a fundamental policy since the thirties, and like every other industrialized nation that has a commitment to such things as housing, and this is what the Congress is facing at this time—whether we reaffirm this national commitment or do not.

Anyway, Mr. Chairman, we ought to give you a chance, but as far as I am concerned—well, I think we are about done.

Mr. **St Germain**. I think the words have been spoken, and we appreciate the testimony of the witnesses. I am hopeful that they will read over my opening remarks and my second opening remarks, and hopefully get the message, so that we can work together.

Mr. **Green**. We look forward to it, sir. Thank you very, very much.

Chairman **Gonzalez**. Gentlemen, thank you for an excellent presentation and your presence and the time you have given us, and the subcommittee will stand in recess until 2 p.m. when we will have the second afternoon panel.

Mr. **St Germain**. If I may, Mr. Chairman, I would ask a little cooperation from the witnesses and the spectators. We do need this room for another function that has been delayed because the hearing went a little later than anticipated, and we will probably start the second hearing at 2:15, if the Chairman doesn't mind too much.

Chairman **Gonzalez**. In other words, what you are telling us is to get the devil out of here as soon as possible.

Mr. **St Germain**. All but the members.

[Whereupon, at 1:40 p.m. the subcommittee recessed for lunch, to reconvene at 2:15 p.m. the same day.]

AFTERNOON SESSION

Chairman **Gonzalez**. The subcommittee will please come to order. This afternoon we resume the hearings and we are honored to have a very distinguished panel this afternoon. We have Ms. Gale Cincotta, the chairperson of the National People's Action; Mr. Ralph Nader of the Public Interest Research Group; Mr. Hall Sisson, of the Communications Workers of America, CWA; Mr.

Martin E. Sloane, the executive director of the National Committee Against Discrimination in Housing.

Let me first express the gratitude of both the staff and the subcommittee for your willingness to accept and donate your time and efforts and energy to be with us. I think we all recognize that it is a very critical time. Some of you I know, if not every one of you, has been very diligent all along in not only this area but related areas of tremendous endeavor.

We were delayed because of the fact that we kind of ran over a little bit on the morning hearing, and also, the majority side of the subcommittee had a caucus in between, so that we apologize for the lateness of the start.

If there is any member of the panel that has some kind of a time emergency that is needed to comply with, some other commitment, or an airplane to catch—I think Mr. Nader has indicated he has that kind of restriction; so, if there is no objection, we will recognize Mr. Nader first.

STATEMENT OF RALPH NADER, PUBLIC INTEREST RESEARCH GROUP, ACCOMPANIED BY JONATHAN BROWN

Mr. Nader. Thank you very much, Mr. Chairman and members of the subcommittee. I would first like to submit for the record a joint statement on H.R. 5568 which has been supported by ourselves, the Communication Workers of America and the National Committee Against Discrimination in Housing, and there will be many other organizations all over the United States who we feel confident will support this statement.

[The joint statement referred to follows:]

March 18, 1982

Member
House Banking Committee
Subcommittee on Housing
U.S. House of Representatives
Washington, D.C. 20515

Re: Joint Statement on H.R. 5568,
the Home Mortgage Capital Stability
Act

Dear Representative:

The undersigned organizations submit the attached Joint Statement on H.R. 5568 in conjunction with individual testimony scheduled for presentation before the Subcommittee on Thursday, March 18, 1982.

H.R. 5568, the Home Mortgage Capital Stability Act, would authorize $7.5 billion of federal capital assistance for institutions that have net worth below 2% of assets and losses for two consecutive weeks. Capital assistance would be in the form of federal loans or capital guarantees.

It is our common position that massive federal capital assistance for savings and loans and savings banks can be justified only if accompanied by specific requirements that mandate a continued role for these institutions as mortgage specialists. This renewed mortgage mandate must generally apply to all savings and loans and savings banks, not just those receiving federal assistance at any given time. Absent this permanent, across-the-board mortgage mandate, the federal assistance provided for in H.R. 5568 cannot be supported.

Specifically, we urge the Subcommittee to incorporate into the proposed legislation the guidelines discussed in the joint statement. First and foremost of these guidelines is a requirement that savings and loans and savings banks invest at least 50% of their total assets in long term mortgages that are either fixed rate mortgages or adjustable rate mortgages with reasonable constraints on rate increases. The rate increase limitations we are proposing are similar to those endorsed last summer by a coalition of more than sixty national and local neighborhood, consumer, labor, and civil rights groups. This single portfolio requirement would accomplish two key goals -- maintaining S&Ls and savings banks as mortgage specialists and assuring a supply of mortgages that do not impose unreasonable risks on homeowners. At the same time the requirement would give savings and loans and savings banks investment flexibility.

H.R 5568 provides a capital assistance mechanism that is generally adequate and wisely steers clear of the overreaching demands of the savings and loan and savings bank industry for massive, non-recoverable operating subsidies for virtually all institutions, regardless of financial condition. However, the bill fails to provide for meaningful mortgage related public benefits. As such, H.R. 5568 cannot be supported unless its public benefits requirements are considerably strengthened.

Respectfully submitted,

Communication Workers of America
National Committee Against
Discrimination in Housing
Ralph Nader

JOINT STATEMENT ON H.R. 5568
A BILL TO AUTHORIZE CAPITAL ASSISTANCE FOR SAVINGS AND LOANS AND SAVINGS BANKS

OVERVIEW

H.R. 5568, the Home Mortgage Capital Stability Act, seeks to address the fact that high interest rates are undermining the viability of a growing number of savings and loans and savings banks. The bill would authorize $7.5 billion of federal capital assistance for institutions that have net worth below 2% of assets and losses for two consecutive quarters. The capital assistance would be in the form of federal loans fully repayable with interest. The House Banking Committee is also considering an alternative approach to assistance that would rely on federal capital guarantees, rather than cash infusions. Either approach raises a fundamental question as to whether there will be public benefits of sufficient magnitude to justify such massive federal assistance. At a time when harsh cuts in federal social expenditures and federal credit budgets are reducing vital services to millions of Americans, clear and compelling public benefits are required before large scale federal assistance to the savings and loan and savings bank industry can be supported.

Public benefit requirements for savings and loans and savings banks must necessarily relate to the traditional role of these institutions as mortgage specialists. Although some redefinition of this role is warranted in light of the phase out of deposit rate controls, there is still a broad public interest in maintaining savings and loans and savings banks as mortgage specialists. It is important to have a set of depository institutions that are mortgage specialists in order to help stabilize the flow of mortgage credit and even more importantly to provide instruments with which to implement federal mortgage credit policies. For example, the Federal Home Loan Bank Board's $65 billion cash advance system supports the mortgage market by means of loans to mortgage specialists. On the other hand, if savings and loans and savings banks are not subject to a redefined, but still strong, mortgage mandate, there is no justification for large scale federal aid to maintain them, and they may just as well be merged with commercial banks.

H.R. 5568 provides a capital assistance mechanism that is generally adequate and wisely steers clear of the overreaching demands of the savings and loan and savings bank industry for massive, non-recoverable operating subsidies for virtually all institutions, regardless of financial condition. However, the bill fails to provide for meaningful mortgage related public benefits, and thus fails to pass the public benefit test. As such, the bill cannot be supported unless its public benefit requirements are considerably strengthened.

THE NEED FOR A NEW MORTGAGE MANDATE

A redefined mortgage mandate for savings and loans and savings banks should serve three important needs. First, it is essential to continue the role of savings and loans and savings banks as mortgage specialists. While these institutions may need added asset flexibility in light of deposit rate deregulation, there is no reason to abandon their role as mortgage specialists. Savings and loans and savings banks have traditionally held a high percentage of their total assets in residential mortgage loans--at year end 1980, 73% for S&Ls and 49% for SBs or, including mortgage backed securities, 77% for S&Ls and 57% for SBs. However, federal law contains no statutory minimum portfolio requirement for savings and loan or savings bank investment in residential mortgage loans. Savings and loans and savings banks are currently under strong pressure to expand into other, short term lending. The incentive to maintain a high percentage of total assets in residential mortgage loans provided by the bad debt deduction provision of the federal tax code will be greatly diminished as a result of current losses and the development of alternative tax shelters, such as leasing. In view of this, it is essential to establish an express statutory minimum portfolio requirement for savings and loan and savings bank investment in residential mortgages.

The second basic need is a continued supply of mortgage loans that do not expose home owners to excessive interest rate risk or refinancing uncertainty. Unfortunately, the mortgage market is shifting rapidly to adjustable rate mortgages that shift most, if not all, interest rate risk to home owners and to short term balloon mortgages that create refinancing uncertainty as well as shifting interest rate risk. If a supply of long term mortgages with reasonable limits on rate increases is not maintained, home ownership will become more difficult and uncertain for millions of Americans in future years. The recent experience in Canada where many home owners with short term rollover mortgages have been unable to absorb sharp payment increases provides stern warning of this peril.

The third goal is to strengthen federal agency oversight of the obligation of savings and loans and savings banks to serve the mortgage credit needs of their entire local community, including low and moderate income areas, older urban neighborhoods, and minorities. This underlying charter obligation was made explicit when Congress enacted the Community Reinvestment Act. Yet, as banking deregulation unfolds, there is a growing trend on the part of many financial institutions to orient their services toward so called "upscale" customers, that is, more affluent persons. Strong oversight will be needed to assure that savings and loans and savings banks continue to serve all segments of the local community.

SPECIFIC REQUIREMENTS OF A NEW MORTGAGE MANDATE

Federal assistance for savings and loans and savings banks cannot be justified unless it is accompanied by specific requirements that will establish a new mortgage mandate for these institutions. To be effective these requirements must generally apply to all savings and loans and savings banks, not just those that are receiving federal assistance at any given time. A mortgage mandate limited to the weakest institutions and confined to the period during which they are dependent on federal assistance would be ineffective. Absent an across-the-board and permanent mortgage mandate, federal assistance cannot be supported.

First and most important there must be a requirement that savings and loans and savings banks invest at least 50% of their total assets in long term mortgages that are either adjustable rate mortgages with reasonable constraints on rate increases or standard fixed rate mortgages. To satisfy this requirement an adjustable rate mortgage should be constrained so that monthly payments cannot increase at a rate greater than two-thirds the average wage increase rate for U.S. workers and, if negative amortization is used, the loan balance cannot increase at a rate greater than one-fifth the inflation rate or the national average home appreciation rate, whichever is less. These ARM constraints would protect the great majority of households against payment increases beyond their budgets and greatly reduce the likelihood of negative amortization causing an erosion of home owners' equity. This single portfolio requirement would accomplish two key goals--maintaining savings and loans and savings banks as mortgage specialists and assuring a supply of mortgages that do not impose unreasonable risks on home owners. At the same time the requirement would give savings and loans and savings banks important investment flexibility. They would be able to invest up to 50% of their assets in non-mortgage loans, commercial mortgages, and residential mortgages not subject to the statutory constraints.

Second, the Federal Home Loan Bank Board (FHLBB) and the Federal Deposit Insurance Corporation (FDIC) should disclose their Community Reinvestment Act (CRA) performance evaluations and ratings for individual savings and loans and savings banks. These agencies currently conduct regular CRA examinations to assess the extent to which institutions have met their obligation to serve the mortgage credit needs of their entire community. Unfortunately, the agencies have refused to disclose these CRA evaluations and ratings. Disclosure, by permitting meaningful public review and comment, would greatly improve the evaluation process, which after all is dependent upon a good working knowledge of local mortgage credit needs. It is inconsistent with a strong public purpose mandate for these evaluations and ratings to remain hidden from public view.

Third, savings and loans and savings banks organized on a mutual basis should be encouraged to retain their mutual form because mutual ownership will prove to be a valuable tool of public mortgage policies in an increasingly deregulated financial environment. Mutual savings and loans and mutual savings banks are better suited than stock institutions to absorb the interest rate risk associated with long term mortgage lending on terms that protect home owners from excessive risk. Stock institutions, which inevitably seek favorable review by stock markets and a high return on stockholders' equity, are under strong pressure to stabilize earnings and to lower capital ratios. This will result in a strong inclination on their part to avoid all interest rate risk, either by emphasizing short term lending or by shifting all interest rate risk to borrowers. By contrast, mutuals can better tolerate earnings fluctuations, so long as their long run viability is not threatened. In view of this public benefit, steps should be taken to strengthen the accountability of mutuals to their members and avoid any large scale conversion of savings and loans or savings banks from mutual to stock form of ownership. Specifically, all federally insured mutual savings and loans and savings banks should be required to (1) obtain express member approval before merging with another institution or converting to stock form, (2) fully disclose to members all compensation paid to management, and (3) prepare an annual report summarizing their mortgage lending, by type of mortgage, over the preceding year. Also, mutual savings and loans and mutual savings banks that are receiving federal capital assistance should not be permitted to convert to stock form until all assistance has been repaid.

INADEQUACY OF THE MORTGAGE REQUIREMENT PROPOSED IN H.R. 5568

In its present form H.R. 5568 has only one express public benefit requirement. This is the requirement that institutions receiving capital assistance must use 50% of their net new deposits to make mortgage loans with an interest rate 1% above their average cost of funds for the purchase of moderately priced homes by first time home buyers. It may be appropriate to impose on savings and loans and savings banks a duty to provide mortgage credit to low and moderate income persons at below market rates. However, this single public purpose requirement is extremely weak and in no way constitutes a new mortgage mandate sufficient to justify federal assistance.

First, the requirement applies to only the weakest savings and loans and savings banks and ends as soon as the institution is strong enough to operate without federal assistance. It is somewhat perverse to require below market rate mortgages from only the weakest institutions. Second, the requirement is likely to have little effect over the next few years because it is linked to net new deposit inflows and the weakest savings and loans and savings banks will not be in a strong position to compete for new deposits. In fact, for all savings and loans net new deposits, as defined by H.R. 5568, declined by $25 billion during 1981. Third and most important, the requirement fails to address the fundamental issues of maintaining mortgage specialists and managing interest rate risk.

THE APPROPRIATE CAPITAL ASSISTANCE MECHANISM

The capital assistance mechanism proposed in H.R. 5568 is basically sound, and the legislation would be justifiable if it were amended to include the proposed mortgage mandate requirements. Capital assistance is properly targeted to troubled institutions--those with net worth below 2% and experiencing losses for two consecutive quarters--and is fully repayable with interest. The alternative approach of providing capital guarantees instead of cash infusions may be preferable, if it significantly reduces initial cash outlays.

In sharp contrast to H.R. 5568, the savings and loan and savings bank industry has advanced a proposal calling for massive, non-recoverable federal subsidies. The industry plan would provide a non-recoverable federal operating subsidy to virtually all savings and loans and savings banks, regardless of their financial condition. At current interest rate levels, this subsidy would amount to $7.5 billion per year. In view of the current budget crisis, the industry's proposal can only be characterized as shameless overreaching.

GUIDELINES FOR ASSISTANCE LEGISLATION

Federal legislation to provide capital assistance to troubled savings and loans and savings banks should adhere to the following guidelines:

1. Savings and loans and savings banks should continue their role as mortgage specialists.

2. Federal statutory requirements to serve the mortgage market should apply to all savings and loans and savings banks (both federal and state chartered), not just to those institutions receiving financial assistance.

3. Savings and loans and savings banks should be required to invest at least 50% of their total assets in long term residential mortgages that are either standard fixed rate mortgages or qualifying adjustable rate mortgages.

4. To qualify for the 50% residential mortgage portfolio requirement an adjustable rate mortgage must have rate increase constraints such that the monthly payment cannot increase at a rate faster than two-thirds the average wage increase rate for U.S. workers and, if negative amortization is used, the loan balance cannot increase at a rate greater than one-fifth the inflation rate or average appreciation rate of U.S. homes, whichever is less.

5. The FHLBB and FDIC should be required to disclose their Community Reinvestment Act performance evaluation and rating of individual savings and loans and savings banks.

6. Large scale conversion of savings and loans and savings banks from mutual to stock ownership should be discouraged.

7. All federally insured savings and loans and savings banks with mutual ownership should be required to (a) obtain member approval before merging with another institution or converting to stock form, (b) fully disclose to members compensation paid to management, and (c) make available to members an annual report summarizing their mortgage lending by type of mortgage.

8. Savings and loans and savings banks with mutual ownership receiving federal capital assistance should be prohibited from converting to stock ownership while federal assistance continues.

9. Federal assistance to savings and loans and savings banks should be targeted to institutions with net worth below 2% and experiencing continuing losses.

10. Any federral capital infusions should be repaid in full with interest.

11. Federal assistance should not involve non-recoverable operating subsidies.

12. The federal banking agencies should not approve the supervisory merger of savings and loans or savings banks into commercial banks or bank holding companies, since this would undermine their role as mortgage specialists.

13. The FHLBB and FDIC should disclose all assistance agreements with savings and loans and savings banks.

Mr. **Nader**. Mr. Chairman and distinguished members of the subcommittee, thank you for the opportunity to comment on H.R. 5568, the Home Mortgage Capital Stability Act. I would like to also ask permission to include my testimony as a whole in the record so I can present a more abbreviated version of it at this time.

Chairman **Gonzalez**. Certainly, without objection, so ordered.

Mr. **Nader**. Thank you, Mr. Chairman. It is apparent that the savings and loan industry is in serious financial trouble, certainly not all savings and loans, but more savings and loans than at any time in the post World War II period.

During the second half of 1981, savings and loans as a whole had a return on assets of negative 1 percent, at an annualized rate. Using the Federal Home Loan Bank Board's semiannual report data, we have estimated savings and loan losses for 1982 on the assumption that the 1 percent loss rate continues throughout 1982. This yields a projection that roughly 925 savings and loans with combined assets of $165 billion will have net worth ratios below 2 percent by the end of 1982.

This projection shows some of the 925 savings and loans with positive net worth between 2 percent and zero, but the average net worth for the 925 institutions will be only a scant 0.35 percent. To boost the net worth ratios of these savings and loans up to 2 percent would require a capital infusion of $2.7 billion during 1982. We hope to have a more detailed report on this rather startling data in a few days.

I would like to focus on that part of our testimony which talks about the necessary public benefits which should be added to this legislation if it is to round out the public purpose, as we see it, of congressional decisionmaking.

The most important issue involved in this legislation is not the question of cost, as important as that is, but rather, the future role of savings and loans and savings banks. It makes no sense to provide capital assistance to prop up individual savings institutions and their managements if these institutions are not subject to clearly-defined public purpose requirements. Any serious set of such requirements must center on mortgage lending, since this is the area of great public need, and savings and loans and savings bank expertise.

One might say mission, too.

In the joint statement submitted by several members of this panel we have outlined a set of mortgage requirements that would establish a new mortgage mandate for savings and loans and savings banks. These requirements would assure that S. & L.'s and savings banks serve important mortgage credit needs and at the same time, permit savings and loans and savings banks sufficient asset flexibility to compete successfully in a financial market without deposit rate controls.

Unfortunately, H.R. 5568 lacks any meaningful public benefit requirements. As pointed out in the joint statement, the bill's only public benefit provision, a requirement that troubled institutions make below-market rate mortgages, is weak and somewhat perverse. It is disturbing to find the House Banking Committee advancing a bill, even under the time limits that it envisions for the legislation, that is so bereft of these public benefits.

Treasury Secretary Regan, FHLBB Chairman Pratt and the Senate Banking Committee Chairman Garn have their clear vision of the future role of S. & L.'s and savings banks, which is rapid consolidation, wholesale conversion from mutual to stock ownership, homogenization with commercial banks, real estate development and investment and securities activities.

Unless the committee acts quickly to establish an alternative future, this deregulation vision will soon become a reality. And under the circumstances, the beneficiaries of a capital assistance program would be managements and stockholders of aggressive financial institutions, not depositors, borrowers or local communities.

The grave flaw in H.R. 5568 is the committee's failure to articulate an alternative vision to that of the Regan-Pratt-Garn deregulation troika. Capital assistance legislation cannot be supported unless it delimits the future role for savings and loans and savings banks. That involves specific public benefits, not just financial homogenization, and a breakdown of the separation of commerce and banking.

It is sad that the committee is not using this opportunity to reestablish a meaningful public purpose mandate for savings and loans and savings banks. Legislative realities are such that the savings and loan and savings bank industry generally have sufficient lobbying power to block public purpose requirements. But when the industry is coming to Congress to ask for help, there is great opportunity to incorporate public benefits requirements into legislation.

Here is a summary of the public benefits which should be associated with any capital assistance program representing a major commitment of Federal Government resources. One, that S. & L.'s and savings banks should be required to invest 50 percent of their assets in long-term residential mortgages that are either standard, fixed rate mortgages or adjustable rate mortgages with reasonable constraints on rate increases.

To qualify for this 50 percent portfolio requirement, adjustable rate mortgages should have rate increase constraints such that monthly payments will not rise faster than two-thirds the average wage increase rate of U.S. workers, and if negative amortization is used, loan balances will not rise faster than one-fifth the inflation rate or home appreciation rate.

Second, the Federal Home Loan Bank Board and the FDIC should be required to disclose their Community Reinvestment Act performance evaluation and rating of individual S. & L.'s and savings banks. Disclosure, by permitting meaningful public review and comment, would greatly improve the evaluation process which, after all, is dependent upon a good working knowledge of local mortgage credit needs.

Third, savings and loans and savings banks organized on a mutual basis will prove to be of great public value in an increasingly deregulated financial environment. Mutual institutions are better suited than stock institutions to absorb the interest rate risk associated with long-term mortgage lending on terms that protect homeowners from excessive risk.

This difference occurs because managements of stock institutions are under strong pressure to operate with low capital ratios in order to increase the return on stockholders' equity, and to avoid earnings fluctuations in order to enhance the market value of their stock. Stock institutions will thus have an increasingly strong inclination to avoid interest rate risk. Additionally, mutuals provide a mechanism for control by borrowers and depositors and have the advantage that all earnings are available for reinvestment, since there are no stockholders requiring dividends.

Efforts should be made to discourage any large-scale conversion of S. & L.'s and savings banks from mutual to stock form. Specifically, mutual institutions receiving Federal capital assistance should not be converted to stock form while Federal assistance continues. Any stock institution receiving capital assistance should be automatically converted to mutual form whenever its net worth, excluding Federal assistance, falls below zero.

Also, as outlined in the joint statement, the Federal Home Loan Bank Board should take specific steps to strengthen the accountability of mutual institutions to their members.

I have a proposal to make in conclusion, which is a longer term proposal, but it is the kind that strengthens community shaping of S. & L. decisionmaking power, and increases the opportunity of members of the community to become in their own right consumer specialists or owner specialists in these financial institutions. It is puzzling, in observing the committee year after year dealing with savings and loan issues, why there is so little consideration of the need for a mechanism that would facilitate the coming together of depositors and borrowers who wish to be organized in that capacity.

A simple requirement that savings and loans and savings banks be required to insert in their annual statements to customers a notice written by such a group inviting other depositors and borrowers to join together would vastly enhance the accountability of savings and loans and savings bank management.

A similar model for utility consumers in Wisconsin called CUB or the Citizens Utility Board now has 65,000 members, a full-time staff of experts and its own newspaper. Enclosed are some descriptive samples of the envelope insert and the CUB brochure for inclusion in the hearing record. This is an insert which appears periodically in the electric or telephone or gas bill and people open up their electric bill and out falls this little business reply envelope which says, read this before you pay your bill. And they invite you to join your friends and neighbors throughout the State into a full-time consumer group with a staff which represents their interests before the utility commission and legislature and courts.

It also vastly educates people in utility matters and demystifies utility matters in little meetings around the State where CUB members come to discuss these issues.

There is also pending in the House of Representatives H.R. 5421, the National Telecommunications Consumers Board Act, which is designed to help telephone consumers organize themselves into a consumer group. And this is now pending.

These mechanisms, Mr. Chairman, impose no tax burden, they establish no Government agency and they are voluntary for consumers. What they do is provide a convenient way for people to band together and redress the enormous imbalance of power between consumer and corporate officials in the making of policy. That is what encouraged the labor movement years ago to organize, to redress the enormous imbalance of power between management and labor.

If applied to savings and loans and savings banks, this mechanism would lead to accountability in investing other people's money, as Justice Brandeis called bank deposits many decades ago. Thank you. And with permission, I would like to submit these materials for the record, as well.

[The prepared statement of Mr. Nader and the information referred to follow:]

STATEMENT OF RALPH NADER
and
JONATHAN BROWN
before the
HOUSE BANKING COMMITTEE
U.S. HOUSE OF REPRESENTATIVES
WASHINGTON, D.C.
MARCH 18, 1982

Mr. Chairman and distinguished members of the Committee, thank you for the opportunity to comment on H.R. 5568, the Home Mortgage Capital Stability Act. This legislation would authorize $7.5 billion of federal capital assistance for savings and loans and savings banks that have net worth below 2% of assets and losses for two consecutive quarters. Capital assistance would take the form of federal loans fully repayable with interest. The Committee's staff is also considering an alternative approach that would involve capital guarantees rather than loans.

In determining whether capital assistance is appropriate it is important to remember that there may be significant federal expenditures no matter what strategy is used to manage problem savings and loans and savings banks. However, this possibility does not mean that the budgetary implications of H.R. 5568 are not of great importance. The capital assistance program contemplated by the bill would involve multi-billion dollar federal expenditures over the next several years. Even if the bill is amended to substitute federal capital guarantees for federal loans, the assistance program would still expose the federal government to the risk of massive expenditures in the event that institutions with capital guarantees do not survive.

A massive assistance program of this nature, which at bottom is designed to preserve the position of individual private firms and their management, can only be justified if there are well-defined and far-reaching public benefits. It is not enough to argue that the savings and loan industry is a victim of circumstances beyond its control. Thousands of small businesses are being forced to close down because of the same malady--continuing high interest rates--that afflicts savings and loans and savings banks, and yet no federal aid is forthcoming.

Unfortunately, H.R. 5568 does not include meaningful public benefit requirements for savings and loans and savings banks. In particular, it fails to establish a new mortgage mandate for these institutions. What is needed is a set of requirements that would serve vital mortgage credit needs of the public and at the same time give these institutions the flexibility needed to compete in an environment without deposit rate controls. In summary, H.R. 5568 fails the public benefit test, and cannot be supported unless substantially amended.

MANY SAVINGS AND LOANS AND SAVINGS BANKS FACE SERIOUS FINANCIAL DIFFICULTIES

There is no question that savings and loans and savings banks are suffering large losses. During 1981 savings and loans had an aggregate loss of $5 billion, while savings banks as a group lost over $1 billion. Savings and loan losses for 1982 are likely to range between $6 billion and $12 billion. Even if short term interest rates were to fall significantly, savings and loan earnings would not recover immediately. A growing share of their deposits are longer term deposits, such as the 30 month certificate, with rates of 13%, 14%, and 15%, and the interest rate on these funds will remain fixed for many months. In addition, the ongoing and necessary phase-out of deposit rate controls will continue to exert upward pressure on the cost of funds, regardless of the course of interest rates. If the savings and loan industry loses $10 billion in 1982, then the industry's aggregate net worth will have declined from $33 billion at year end 1980 to $18 billion by year end 1982.

However, such aggregate net worth data obscures the important fact that some savings and loans and savings banks have very weak net worth positions, while others are still relatively strong. A review of the semiannual reports that savings and loans file with the Federal Home Loan Bank Board (FHLBB) shows that as of June, 1981, 189 savings and loans with combined assets of $25 billion had net worth to asset ratios below 2%. Yet, the 2,756 savings and loans with net worth ratios above 4% had an aggregate net worth ratio of 5.79%, a reasonably healthy capital cushion. Any federal assistance program should be targeted to institutions with weak net worth positions.

During the second half of 1981 savings and loans as a whole had a return on assets of negative 1%, at an annualized rate. Using the FHLBB's semiannual report data, we have estimated savings and loan losses for 1982 on the assumption that the 1% loss rate continues throughout 1982. This yields a projection that roughly 600 savings and loans with combined assets of $110 billion will have net worth ratios below 2% by the end of 1982. This projection shows some of the 600 savings and loans with positive net worth (between 2% and 0), but the average net worth for the 600 institutions will be only negative 0.3%. To boost the net worth ratios of these savings and loans up to 2% would thus require a capital infusion of $2½ billion during 1982.

ALTERNATIVES TO CAPITAL ASSISTANCE ARE NOT WITHOUT COSTS

The cost to the FSLIC and FDIC insurance funds, and ultimately to the federal government if these funds prove inadequate, of a large number of savings and loan and savings bank failures would be substantial. Most savings and loan and savings bank deposits are insured by FSLIC or FDIC, and a case can be made that, under the present circumstances, it is prudent for the insurance funds to continue their present policy of covering uninsured deposits in order to prevent major deposit withdrawals. When institutions fail the insurance funds must pay off depositors and take over mortgage assets with greatly depreciated market values. FSLIC Director Brent Beesley has estimated the average cost to the FSLIC of liquidating failed savings and loans to be about 30% of the failed institutions' assets. The recent Brookings Institution study of savings and loans and savings banks estimated the market value of these institutions' assets to be 14% below their book value.

Rather than undertake costly liquidations, the FSLIC has merged failing savings and loans into other savings and loans. However, such distress mergers can require substantial assistance payments from the FSLIC. For example, FSLIC estimates the cost of the 7 FSLIC assisted mergers arranged during the first five months of 1981 to have averaged 22% of the assets of the merged savings and loans. In recent months FSLIC has held out the carrots of interstate banking and purchase accounting procedures designed to disguise current losses in order to reduce the assistance demands of savings and loans submitting bids for distressed savings and loans. According to FSLIC data that strategy has had some success. FSLIC's cost for the 16 supervisory mergers arranged during the last seven months of 1981 averaged only 5% of merged assets. However, this data should be treated with caution because it involves very speculative estimates of the present value of future FSLIC payments which themselves are contingent on interest rate changes.

In any case, considerable doubt exists as to whether FSLIC can continue to arrange an ever increasing number of supervisory mergers at such low assistance costs. As more savings and loans encounter earnings difficulties, there are fewer savings and loans strong enough to absorb the failures.

Also, many troubled savings and loans are located in markets that other savings and loans are not interested in entering, even on an interstate basis.

In an effort to hold down the cost of assisted mergers, the FDIC and FHLBB, with Federal Reserve Board approval, are likely to authorize large bank holding companies to acquire failing savings and loans and savings banks across state lines. Such an approach is consistent with the Reagan Administration's position that savings and loans and savings banks should be given full commercial bank powers and the depository institution system homogenized. However, caution must again be exercized in evaluating this approach because no one knows whether commercial banks would be willing to acquire a great number of failing savings and loans without substantial FSLIC assistance.

Although predictions are perilous, it is quite possible that the FSLIC's $6.8 billion insurance fund will have to be supplemented with additional federal appropriations over the next few years. Thus, there are really two alternatives for addressing the current situation. One is to continue with an expanded supervisory merger program and enact legislation giving the FSLIC a much greater line of credit with the Treasury Department. The other approach, as proposed by H.R. 5568, is to augment the existing insurance fund with a capital assistance fund. If interest rates turn upward in future years and many savings and loans and savings banks fail in spite of capital assistance, then the capital assistance approach will undoubtedly cost more than an assisted merger approach. On the other hand, should interest rates fall significantly and many troubled savings and loans and savings banks recover, a capital guarantee approach could well cost less than the assisted merger approach.

THE BILL IS VOID OF NECESSARY PUBLIC BENEFITS

The most important issue involved in this legislation is not the question of cost, but rather the future role of savings and loans and savings banks. It makes no sense to provide capital assistance to prop up individual savings institutions and their managements if these institutions are not subject to clearly defined public purpose requirements. Any serious set of such requirements must center on mortgage lending, since this is an area of great public need and savings and loans and savings bank expertise. In the Joint Statement submitted by several members of this panel we have outlined a set of mortgage requirements that would establish a new mortgage mandate for savings and loans and savings banks. These requirements would assure that savings and loans and savings banks serve important mortgage credit needs and at the same time permit savings and loans and savings banks sufficient asset flexibility to compete successfully in a financial market without deposit rate controls.

Unfortunately, H.R. 5568 lacks any meaningful public benefit requirements. As pointed out in the Joint Statement, the bill's only public benefit provision--a requirement that troubled institutions make below market rate mortgages--is weak and somewhat perverse. It is disturbing to find the

House Banking Committee advancing a bill that is so bereft of public benefits.

Treasury Secretary Regan, FHLBB Chairman Pratt, and Senate Banking Committee Chairman Garn have a clear vision of the future role of the savings and loans and savings banks--rapid consolidation, wholesale conversion from mutual to stock ownership, homogenization with commercial banks, real estate development and investment, and securities activities. Unless the Committee acts quickly to establish an alternative future, this deregulation vision will soon become a reality. Under these circumstances, the beneficiaries of a capital assistance program would be managements and stockholders of aggressive financial institutions, not depositors, borrowers, or local communitites.

The grave flaw in H.R. 5268 is the Committee's failure to articulate an alternative vision to that of the Regan-Pratt-Garn deregulation troika. Capital assistance legislation cannot be supported unless it delimits a future role for savings and loans and savings banks that involves specific public benefits, not just financial homogenization and a break down of the separation of commerce and banking. It is sad that the Committee is not using this opportunity to re-establish a meaningful public purpose mandate for savings and laons and savings banks. Legislative realities are such that the savings and loan and savings bank industry generally has sufficient lobbying power to block public purpose requirements. But when the industry is coming to Congress to ask for help, there is great opportunity to incorporate public benefit requirements into legislation.

NECESSARY PUBLIC BENEFITS

A summary of necessary public benefits is provided below. Absent these public benefits, a capital assistance program would represent a major commitment of federal government resources without commensurate public benefit.

1. Savings and loans and savings banks should be required to invest 50% of their assets in long term residential mortgages that are either standard fixed rate mortgages or adjustable rate mortgages with reasonable constraints on rate increases. To qualify for this 50% portfolio requirement, adjustable rate mortgages should have rate increase constraints such that monthly payments will not rise faster than 2/3 the average wage increase rate of U.S. workers and, if negative amortization is used, loan balances will not rise faster than 1/5 the inflation rate or home appreciation rate. Savings and loans and savings banks could invest the remaining 50% of their assets in non-mortgage loans, commerical mortgages, and residential mortgages not subject to the statutory constraints. This would give these institutions important investment flexibility, and at the same time provide a supply of mortgages that do not impose unreasonable risk on home owners.

It is often asserted that constraints on adjustable rate mortgages will lead to renewed earnings difficulties for savings and loans and savings banks in the future. Yet, Chairman Pratt has provided strong evidence that adjustable rate mortgage constraints even stricter than those proposed above are workable. In July 1981 testimony before the House Banking Committee, Mr. Pratt calculated that if savings and loans since 1975 had been making ARMs with a 1% per year limit on interest rate increases, their 1980 mortgage portfolio yield would be 1.37% higher than it is today. Then Mr. Pratt stated that "the thrift industry would still be profitable today, and the current net worth erosion would be nonexistent," if the 1980 mortgage portfolio yield had been increased by only 1.0%.

2. The FHLBB and FDIC should be required to disclose their Community Reinvestment Act performance evaluation and rating of individual savings and loans and savings banks. Disclosure, by permitting meaningful public review and comment, would greatly improve the evaluation process, which after all is dependent upon a good working knowledge of local mortgage credit needs.

3. Savings and loans and savings banks organized on a mutual basis will prove to be of great public value in an increasingly deregulated financial environment. Mutual institutions are better suited than stock institutions to absorb the interest rate risk associated with long term mortgage lending on terms that protect home owners from excessive risk.

This difference occurs because managements of stock institutions are under strong pressure to operate with low capital ratios, in order to increase the return on stockholders' equity, and to avoid earnings fluctuations, in order to enhance the market value of their stock. Stock institutions will thus have an increasingly strong inclination to avoid interest rate risk. Additionally, mutuals provide a mechanism for control by borrowers and depositors, and have the advantage that all earnings are available for reinvestment, since there are no stockholders requiring dividends. Efforts should be made to discourage any large scale conversion of savings and loans and savings banks from mutual to stock form. Specifically, mutual institutions receiving federal capital assistance should not be converted to stock form while federal assistance continues. Any stock institution receiving capital assistance should be automatically converted to mutual form whenever its net worth (excluding federal assistance) falls below zero. Also, as outlined in the Joint Statement, the FHLBB should take specific steps to strengthen the accountability of mutual institutions to their members.

4. It is puzzling to observe year after year the Banking Committee deal with savings and loan issues without any consideration of the need for a mechanism that would facilitate the coming together of depositors and borrowers as intelligently organized consumers. A simple requirement that savings and loans and savings banks be required to insert in their annual

statements to customers a notice written by such a group inviting other depositors and borrowers to join together would vastly enhance the accountability of savings and loan and savings bank management.

A similar model for utility consumers in Wisconsin--called CUB, or the Citizens Utility Board--now has 65,000 members, a full time staff of experts, and its own newspaper. Enclosed are some descriptive samples of the envelope insert and the CUB brochure for inclusion in the hearing record. There is also pending H.R. 5421--The National Telecommunications Consumers Board Act--designed to help telephone consumers organize themselves into a consumer group.

These mechanisms impose no tax burden, establish no government agency, and are voluntary for consumers. What they do is provide a convenient way to band together and redress the enormous imbalance of power between consumer and corporate officials in the making of policy. If applied to savings and loans and savings banks, they would lead to accountability in investing "other people's money."

CUB

CITIZENS
UTILITY
BOARD

Here's what you
can do about
rising utility rates.

CUB Campaign
P.O. Box 19312
Washington, D.C. 20036
202-387-8030

You know the old story:

Electric, gas and telephone bills just keep going up and up.

Your only choice is to dig deeper into your pocket to pay the bill, or turn off the lights, right?

Wrong.

Now there's something people can do to help themselves:

Form a **Citizens Utility Board**, or **CUB**.

That's what over 50,000 people are doing in Wisconsin. Now they can work for fair utility rates.
Now consumers can challenge the utilities, and balance the process.

Here's how.

CUB: A balancing act

The Problem:

Everybody knows that electric, gas and telephone rates keep going up. Utilities can cause other problems as well — their rates are often biased against small users, their service policies are sometimes unfair, and they occasionally build unnecessary power plants. And we know how hard it is for people to challenge giant utility companies — whether it's about a rate increase, a service complaint, or the location of a new plant. The lone citizen is simply no match for the utilities' lobbyists, lawyers, and experts.

And of course, if you don't like your utility company, you can't shop around.

So what can you do?

A New Solution—The Citizens Utility Board (CUB)

In Wisconsin, people have developed a new way of doing something about utility rate increases and problems — and it's an idea that could work in any state in the country. They are forming a Citizens Utility Board, or CUB, which will represent residential consumers on electric, telephone, gas and water issues. Whenever regulatory agencies, the legislature or other branches of government make decisions about the cost or quality of utility service, CUB will be there to make sure consumers' views are heard.

In less than a year, over 50,000 people joined Wisconsin's CUB, contributing an average of $5 each. With these contributions, CUB hired experts to work for consumers.

In most states, the utilities speak out for their interests loud and clear. Now, with CUB, consumers will be heard too. CUB *balances* the process.

How was the Citizens Utility Board created?

The Wisconsin legislature passed a law creating CUB and giving it the right to enclose notices inside monthly utility bills. These notices describe CUB's activities and invite people to join. The right to enclose these notices is vital. This gives consumers the ability to get together, and to pool small amounts of time, money and ideas to challenge the utility companies when necessary. Without this right, CUB could not exist.

"Isn't enough enough?" began a CUB message enclosed in a Wisconsin electric bill. It explained the utility's demand for a 23% increase and invited ratepayers to contribute so CUB could challenge unwarranted aspects of the increase.

It's all because of these enclosures that over 50,000 people have already joined Wisconsin CUB, and membership will keep going up.

What Can CUB Do?

Contributions are used to hire experts — lawyers, accountants, economists and engineers — to work for consumers' interests. CUB can challenge unnecessary or unfair rate increases by presenting expert analysis and questioning the utilities' arguments; and it can propose ways for the utilities to be more efficient. CUB can also investigate the siting of a new plant, or work to change unjust service rules and policies. Because CUB is governed democratically, CUB will work on whatever issues are of the greatest concern to the members.

With CUB, consumers are represented before the state regulatory commission and other public bodies where important decisions are made. **Right now, the utilities spend ratepayers' money to argue their case, but the individual can't afford to represent him or herself. CUB gives consumers clout that they don't have as individuals.**

How Does CUB Work?

CUB is a voluntary organization. It is not a state agency and does not receive any tax dollars. It depends on voluntary contributions. People learn about CUB from the notices inside their bills, and join by contributing a few dollars a year. The members elect a board of directors, who decide what CUB should do and how the money should be spent. (The directors hire staff to carry out CUB's work.) Members also participate in meetings, surveys and other activities.

Because CUB depends on voluntary contributions, it must work for public support. If it doesn't perform, it will die. With this incentive, it cannot become a lazy and wasteful bureaucracy.

And it means people can do something for themselves about inflation without a single tax dollar being spent.

How Can a CUB Be Formed in My State?

A law must be passed creating CUB and giving it the right to enclose notices in utility bills. This is essential. Some legislation also proposes placing a check-off box on the utility bill for contributions. This would make it even more convenient for people to contribute.

To pass a CUB law, you need a broad coalition of support. In Wisconsin, the major consumer, farmer, elderly, labor, minority and church organizations, along with the Democratic and Republican legislative leaders and some Public Service Commissioners, all joined to work for passage of the CUB bill. (See the list of supporters on the back.) Republican Governor Lee Dreyfus signed it into law.

957 **BEST DOCUMENT AVAILABLE**

Who Opposes CUB?

The utilities. They don't want an organization capable of pointing out where they are inefficient or unfair. In Wisconsin, they said CUB was unnecessary because consumers were already represented. They said it would be too costly to enclose the notices. And they prevented the bill from passing for three years.

But people never gave up, and finally won. The fact that over 50,000 people joined Wisconsin CUB in just a few months is proof of its popular support. The law requires CUB to reimburse the utilities for additional costs resulting from the enclosure; in fact, the actual costs of enclosing notices have been extremely low, and they have been paid by CUB. Utility executives have now stated that CUB flyers can be enclosed in monthly bills for a minimal or no cost.

How Can I Help Create a CUB in My State?

Urge your state representative to work on passing a Citizens Utility Board Act. Wisconsin's law is a good model. Tell your friends and neighbors to contact their representatives, and contact consumer, elderly, labor, homeowner, farmer, taxpayer and religious organizations for their support. A broad coalition is needed to take on the utilities.

Wisconsin is the first state in the nation to pass a CUB law. People in several states are trying to do so now, as Wisconsin's CUB proves the idea works.

The CUB Campaign in Washington, D.C. is working with Wisconsin's CUB to provide information to people interested in this new idea. You can obtain copies of the CUB law, utility bill inserts, newspapers, fact sheets and other materials that can answer your questions and help you build support for a CUB. For more information, send a self-addressed stamped envelope to:

CUB Campaign
P.O. Box 19312
Washington, D.C. 20036
202-387-8030

Who supports CUB

CUB legislation has been introduced in a dozen states and has been supported by public officials, consumer, farmer, labor and elderly organizations, church associations, and small business groups.

In Wisconsin, the first state to create CUB, the legislation was sponsored by the leadership of the legislature, supported by Public Service Commissioners Charles Cicchetti and Edward Parsons, and signed by Republican Governor Lee Dreyfus. As the organization began its work, the Governor and the Mayors of Madison and Milwaukee declared November, 1980 as "CUB Month."

In addition, the following organizations have endorsed Wisconsin CUB:

Wisconsin AFL-CIO
Wisconsin Farmers Union
Wisconsin Council of Churches
Wisconsin Retired Teachers Association
Allied Council of Senior Citizens of Wisconsin
Wisconsin Education Association
United Auto Workers, Region 10
AFSCME Councils 24 and 48
Democratic Party of Wisconsin
Retired Property Owners Assn
Center for Public Representation
The Milwaukee *Journal*
The *Madison Capital Times*
and many others

Some comments about Wisconsin's CUB

"CUB provides an excellent opportunity for citizens to fight back against the rising cost of energy. I urge everyone who can't afford to waste money on utility bills to participate in CUB and help it have an impact on our energy future. Our progressive tradition demands citizen involvement, and CUB is an excellent place to exercise it."

—Clifford Krueger, Wisconsin State Senate Minority Leader (Republican)

". . . what if the process hasn't been working all that well? Then this same group of independent experts will uncover productive initiatives for CUB to take — initiatives, I suspect, that will save ratepayers millions of dollars."

—Ed Jackamonis, Speaker, Wisconsin State Assembly (Democrat)

"Utility bills are a big expense for farmers, and one that is getting bigger. I've found that farmers join CUB faster than just about any group I know of, as soon as they know what CUB is about. Family farmers have known for a long time that you've got to be organized to get fair treatment from big companies like utility monopolies."

—Leland Mulder, President, Wisconsin Farmers Union

"CUB gives workers an articulate and strong voice at the Public Service Commission when the big ticket items that make utility rates go up are ruled on. It's not a bureaucracy; it's people working together for fair utility rates."

—Joe Gruber, Executive Vice President, Wisconsin AFL-CIO

". . . perhaps the most creative consumer idea of the last generation."

—Ralph Nader

and on enclosing CUB notices in utility bills:

"The CUB brochure was received in such good condition that it created no problems in our Bill Mailing Unit, and we experienced only nominal additional expenses for the insertion operation for which [CUB] was not billed."

—Carl Koch, Vice President, Wisconsin Telephone Co. (AT&T subsidiary serving 1 million residential customers)

Citizens Utility Board of Wisconsin, PO Box 8003, Madison, WI 53708, (608) 255-2971

This message was written and paid for by the Citizens Utility Board (CUB), *not* the Wisconsin Electric Power Co.

Isn't enough enough?

Your electric bill was increased 15% last year.

Now, Wisconsin Electric, your utility, wants to increase your rates again, by 14%. *That means you could pay $50, $100 or even $200 more for electricity alone this year.*

The Citizens Utility Board wants to challenge this increase. We think it is too much for consumers to pay.

That's why we need your help today. You can join CUB for just $3, $5, or $10. CUB was created by law to represent consumers, but does not receive tax dollars. CUB is funded by your contributions.

If you contribute, CUB will have the resources it takes to challenge Wisconsin Electric's request. When the utility asks the Public Service Commission for the increase, CUB will be there with consumer experts to defend your interests.

And by joining CUB, you'll be joining over 25,000 people who've said they want clout when utility rates are set. We'll be working to try to make sure our electric rates—as well as our telephone, gas and water rates—are fair in the future.

Join CUB today.

Sincerely,

Sharon Chamberlain

Sharon Chamberlain
Director
Citizens Utility Board

Yes! I want to help challenge Wisconsin Electric's rate increase and join the effort for fair utility rates. I want to join CUB.

Name ____

Address ______________________________ City ______________ ZIP ________

Phone ______________________________

Enclosed is my contribution of:

☐$3*　　☐$5　　☐$10　　$_____other

☐I'm already a member. Here's an extra contribution to help challenge Wisconsin Electric.

*Minimum annual per person dues by law. Please contribute more if you can to help make CUB strong.

Make checks payable to Citizens Utility Board

As a CUB member, you'll elect a board of fellow ratepayers who will direct CUB. You will also receive regular information on current rate increase proposals and tips on how you can save on your utility bills. And your contributions will work for fair utility rates all year round.

Chairman **Gonzalez**. Mr. Nader, do you have sufficient time for the question period if we hear the other witnesses, or would you rather that we proceed with the questions directed to you, if you have this kind of time pressure on you. I believe if there is no objection we could proceed that way.

Mr. **Nader**. Yes, I do have an appointment with a U.S. Senator.

Chairman **Gonzalez**. Well in that case, you are not excused.

[Laugther.]

Mr. **Nader**. I was about to confess that there are—pardon me—3 to 5 minutes if you would like, and if the members of the panel don't object.

Chairman **Gonzalez**. If there is no objection on the part of your colleagues on the panel or the members of the subcommittee, I think we, in all fairness, since we did start late, perhaps we can proceed that way.

I am going to defer to the chairman of the full committee because you have presented your views with respect to the one bill introduced by the distinguished chairman, H.R. 5568. And I would like to—if you have not received, I would like to invite your attention and we will send it to you, a copy of the bill, the main vehicle for these hearings, the Housing and Urban Development Act of 1982.

And since this came in on an emergency basis and also has a tie-in with your 50 percent investment in fixed mortgages and the like, this was the quickest way actually to facilitate both things, but actually the expertise and the real jurisdiction with respect to the savings institutions is in the subcommittee that the chairman of the overall committee continues to chair.

But I would like to perhaps involve you at a later date and convenient to you, your participation in our hearings with respect to the specific housing legislation pending also.

Mr. **St Germain**. Thank you, Mr. Chairman. Mr. Nader, with respect to your 50 percent requirement, at the present time, wouldn't that be rather an academic thing in view of the fact that savings and loans are required at the present time to invest 82 percent of their funds in mortgage lending and mutual savings banks, 76 percent?

Mr. **Nader**. Mr. Chairman, first of all, we want to make sure that those that do not reflect the average you just indicated would be covered. And if there isn't that kind of problem, this kind of minimum should not be objectionable. So it is that kind of safeguard.

Mr. **St Germain**. Well, let us put it this way. You can argue that way but I can argue the other way and say that what we are doing here is imposing a requirement. Incidentally, in reading your statement at page 3, any Federal assistance program should be targeted to institutions with weak net worth positions. That is what the legislation does. You have to fall below 2 percent for 2 quarters in order to qualify.

I do not understand that statement on page 3.

Mr. **Nader**. Do you mean on the 50 percent?

Mr. **St Germain**. No. On page 3 of your statement in paragraph 2, you say:

A review of the semiannual reports that S. & L.'s file with the Home Loan Bank Board shows that as of June 1981, 189 S&L's with combined assets of $25 billion had net worth to asset ratios below 2 percent. Yet, the 2,756 savings and loans with net worth ratios above 4 percent had an aggregate net worth ratio of 5.79 percent, a reasonably healthy capital cushion.

I do not disagree with that. I am aware of those statistics. Then you say, "Any Federal assistance program should be targeted to the institutions with weak net worth positions." That is what the legislation does.

The way I read this, it is as though we are attempting to assist institutions with high net worth.

Mr. NADER. But you see, we are trying to anticipate the U.S. Savings & Loan League, which supports, as we understand it, across-the-board assistance, so we are just trying to make clear that we think that is a good provision.

Mr. ST GERMAIN. I could not agree more. Frankly, one of the big reasons is that we just cannot afford to go out there and help everybody. And I think it is important to help those who need the assistance, not just anyone at all. We intend to, incidentally, write the criteria in such a manner we are going to expand on the criteria for the insuring agencies who would be making the decisions here to insure that the institutions that are assisted do indeed have good management and that they indeed can survive if assisted. So it is not throwing good money after bad.

As you have alluded to in your statement, we additionally are going to provide net worth guarantee certificates instead of cash. We will go through the appropriations process, however, with no outlays The only time there would be an outlay is if an institution that had a net worth guarantee certificate were to fail.

Hopefully, that will not happen if the process is properly structured because there will be reasonable opportunity or there will be reasonable hope that the institutions assisted will survive.

I would like to make this other point, Mr. Nader. I am sure you are aware of the fact that redlining legislation would not be on the books if it were not for this member. I carried that pail of water when I was the only one, and then was eventually assisted by other members of the committee, but it was a tough fight. So I think my record is pretty clear in areas of public interest.

However, this legislation I did not view as a vehicle for public interest legislation to be added. If you viewed or have had an opportunity to look at the principles that we annunciated for our hearings in the FIRA document which is our answer to what you referred to as the troika legislation on the other side, you will find that everything that you listed in your joint statement is contained therein.

If we were to add some of these items that you wish added here, frankly I think what they would want to do is send the bill back with the troika legislation as a rider. I frankly feel that if we are going to be successful in aiding thrift institutions that are in dire difficulty, and hopefully maintaining a system to provide home mortgage funds, that this is an interim step that must be taken.

But I do not look upon this legislation as the answer to all problems and I do not contend that it is. It was not drafted for that purpose. We did incorporate the 50-percent requirement for home mortgage lending to first-time home purchasers for residential mortgages. We felt that that was a necessary component. Otherwise, we would not want to see this go the route of the all-savers certificate where the funds there were used to purchase security, mortgage-backed securities, that created no new housing whatsoever. That was a farce and I do not want to see that repeated.

So with that, I will not ask any questions. I just thought I would make my position clear on that.

Mr. **Nader**. Mr. Chairman, we think that you have exceptional bargaining power whenever you are dealing with subsidy legislation that the industry wants—whether it is S. & L.'s or other subsidy legislation outside the banking area—to attach these public benefits. I am very glad to see that you have already been on the record as supporting all of these. So really, it is a request for a tactical consideration.

Mr. **St Germain**. Ralph, we have been that route before. As to tactical considerations, I always have appreciated your input and I think Mr. Sisson was at some of those meetings as well as another gentleman back there, and so I will very definitely take your recommendations into consideration.

As to the ultimate tactical decisions, I am going to have to reserve those and hope that I do what is best.

Mr. **Nader**. That goes without saying. You people are the lawmakers, but it is our judgment that when you are giving an industry something—and you are giving them something very valuable—that you can condition it.

I think the integrity of the subsidy process across the board in our Government has been undermined by a kind of one-way approach giving but not conditioning. And we need to establish——

Mr. **St Germain**. Here is where we may disagree. I do not look upon this as giving to the industry. Frankly, it is not the industry that concerns me; it is the prospective home purchaser that concerns me. I am concerned about the fact that we may not have a delivery system for home mortgage financing. That is what concerns me.

I am concerned about the people I met in Seattle, Wash., who have been out of work now for over 1 year because the saw mills have shut down and they are no longer cutting trees. I am concerned about the people in Atlanta who are out of work because they are not manufacturing carpets. The hardwood industry has closed down; they are not making furniture. People in Chicago that are out of work because they work in industries that are dependent upon home purchases.

Therein lies my concern. It is not with the S. & L., individual S. & L.'s or the U.S. League of Savings Associations or the National Savings & Loan League. It is with the people that I feel would benefit if we are able to insure that these institutions survive, and that they are required to put money into home mortgage lending.

Mr. **Nader**. I think there is no disagreement there. What our proposals are designed to do is to further insure that, and to give more data and information to community groups so they can carry some of the burden on their shoulders, too, and not just leave it up to Congress and the Federal Home Loan Bank Board, the latter being now in rather dubious hands.

As far as the needs of middle and lower income people are concerned for housing—and I am sure other members of the panel will drive that point home—I think that is really what emanates these public benefit conditions. Because so often when programs come out of here, they are designed to help not just the immediate industry but, as you say, the workers and other parts of the economy. But they never dribble all the way. I mean there is a lot of leakage and a lot of seepage on the way, and to try to minimize that really represents the purpose of these public benefit amendments.

Mr. **St Germain**. Well, we thank you for your concern and your suggestions and your submissions.

Mr. **Nader**. Thank you.

Mr. **St Germain**. Thank you, Mr. Chairman.

Mr. **Bethune**. Mr. Nader, if I could just have a couple of minutes of your time. First, I detect from the overall tone of the testimony that your basic purpose is to raise what I consider very thoughtful questions, and they are: If Congress is to pass some sort of assistance program for the S. & L. industry, what is going to happen with the money, where is it going to wind up and who is it going to benefit. And I think these are critical questions.

You raise two subparts to these questions, as I see it: One, about the long-term role for the savings and loan industry—are they going to get into something other than housing, and if they are what is it going to be, and who is that going to benefit? And I think that is a legitimate question.

And second, you raise questions about the form of the business entities that are out there right now, the question being whether or not aid might have a better chance of filtering down to people who need housing or whether or not it might be siphoned off in the case of a stock organization. And I think that is a legitimate question. This morning we heard from the industry people, and these were the same two thoughts that kept going over in my mind all morning long:

One, where are we going in the long term with this industry? Are we going to have an amalgamation of S. & L.'s, banks, and some other entities? What does that mean, because we are talking about a sizable amount of money here at a time when we are trying to find places to save money rather than spend it?

Then, second, the question that I kept hearing this morning was: What conditions or limitations should be placed on who qualifies and who does not qualify for this assistance. And it kept occurring to me, who is it we are trying to help here.

In fact, I even began to think in reverse: Should we not be helping the industries that are attracting savings, those institutions out there that are doing well, that are actually making housing loans right now, and let the others merge out?

So I think it is good that you have raised these questions here. I say all that just as a compliment, basically, to the thrust of your testimony.

Next, am I not mistaken—or am I not correct that you were opposed to the Chrysler bailout?

Mr. **Nader**. Yes, without conditions. I testified——

Mr. **Bethune**. I did not have the benefit of hearing your testimony.

Mr. **Nader**. It was the same principle, that if you are going to bail out the company because it will help other people, like workers, then let us establish some conditions to make sure that it is likely to work and to make sure that the public receives some byproduct of the benefits. In this case they dealt with certain engineering advances in mass transit and auto safety which Chrysler had been working on in a small way for the Federal Government.

You see, by definition subsidy assistance programs always get caught up in a hurry, hurry up. There is a no-time-to-lose atmosphere on Capitol Hill, and that militates against solid consideration of conditions. Obviously you up there look at it from a different perspective of urgency and practicality than we do here, which is why we have to be here. That is the whole point.

Mr. **Bethune**. I would encourage you—I do not think your organization has yet—to look at the entire credit budget proposition that Norman Mineta and I are working on in an effort to try to make sense out of this overall problem of credit assistance programs. This one will wind up looking very much like a credit assistance program when we get through with it, I would expect. I already see the term "loan guarantee" cropping up here and there, but I will send you a package of material on that and I would encourage you to take a good look at it.

And then finally, I would just like to say that I am not sure that you and I wind up in agreement on too many things, but we did agree on Chrysler.

And then recently the Alaska Natural Gas Pipeline was a matter of some importance around here, and I would just like to compliment you for an excellent piece of work on that.

Mr. **Nader**. Thank you.

Mr. **Bethune**. Thank you, Mr. Chairman.

Mr. **St Germain**. Mr. Chairman, if I might make a point. Incidentally, on the legislation, it does state that in the case of a stock organization no dividends will be paid during that period of time that the institution has a net worth guarantee certificate.

Chairman **Gonzalez**. If you have a little time, Ms. Oakar may have a question. Ms. Oakar and Mr. Vento?

Mr. **Vento**. I have no questions.

Ms. **Oakar**. I just had a parenthetical situation. I would just like you to comment briefly on it, Ralph, if you can. Suppose we have the situation of the individual who has paid off a house for 12 years on, let us say, a 20-year mortgage and missed two payments, but did—and I am really speaking of some specific cases that have come by my desk relative to some people who live in the suburbs of Cleveland, pay the interest on those two payments.

But now the bank or the S. & L., I should say, is saying that they either lose their home or they jump from a fixed rate of interest of 9 percent to 14 percent, which means they are out of the ball park, because if they could not afford the 9 percent they are never going to afford the 14 percent.

Do you think this legislation as it is or with some amendments would allow this S. & L. more flexibility toward that kind of person, or would we still see the same kind of rather cavalier situation that at times has gone on in the past?

Mr. **Nader**. Well, I think the way it is written it does not restrain the S. & L. in the kind of case that you just described. That is why we also favor improving the bargaining power of people in the communities, because it is hard to cover all of these contingencies in legislation. It is even harder to get these contingencies which are covered, enforced by an administrative regulatory agency.

But if you had an organization of borrowers and depositors, then you could have rather routine meetings, for example, with bank management to try to work out a lot of these issues on a negotiation basis. There is just no way, even if you have a terrific person, even if Congressman St Germain headed the Federal Home Loan Bank Board, there is no way that you can get down to the grassroots level.

That is why we have made this proposal apropos the utility envelope in Wisconsin. We have got to have more organized mechanisms to facilitate banding together by people in communities, whether they are consumers of automobiles or insurance or utility services or banks.

Ms. **Oakar**. Thank you, Mr. Chairman.

Chairman **Gonzalez**. Mr. Nader, on page 2—this is the only question I am going to ask, because I would submit it in writing, but since you are here—and it has reference to this sentence on page 2, the second paragraph, the second sentence: "In particular, it fails to establish a new mortgage mandate for these institutions."

Well, I have been under the impression that that was exactly what the chairman had explained to me it would do. Could you elaborate on that?

Mr. **Nader**. Let me have John Brown elaborate on this, because this is his favorite area that he has worked on.

Mr. **Brown**. Mr. Chairman, the meaning behind the statement that there is no new mortgage mandate was simply that the only condition to serve the mortgage market in the present bill applies to the institutions receiving assistance, and it only applies for the duration of the period that they are receiving assistance. So that there is no across-the-board mandate that applies to the savings-and-loan industry.

Now, as we discussed in the joint statement, the requirement in the bill that would apply to troubled institutions is very weak and we do not think it is a very effective mandate. So on both scores, the fact that the requirement is weak and the fact that it does not apply across the board, we feel that there is just generally no overall direction delimiting a future role for savings and loans in the bill.

One further comment. The point was raised by the chairman that our proposal that the savings and loans would have to invest 50 percent of their assets in mortgage loans with safeguards on them did not really introduce anything new, because most S. & L.'s are already at that level, is not quite accurate. What we are proposing is that 50 percent of their assets be in mortgages with safeguards. The present situation right now is that there are no safeguards of this type on any of their mortgages.

S. & L.'s could impose safeguards voluntarily if they wanted to, but the Bank Board about 1 year ago totally deregulated safeguard requirements on the mortgage instrument. So right now savings and loans can invest 100 percent of their assets in mortgages with no safeguards at all.

And I think, in reference to the previous testimony concerning the homeowner in a position of having rate increases which they cannot bear, you can see that requiring savings and loans to invest 50 percent of their assets in mortgages with safeguards would be a very significant benefit and a very great improvement over the present situation.

Chairman **Gonzalez**. Well, the thing is that it does provide a mandate. Your statement is categorical. It says, "In particular, it fails to establish." Now, you do use the words "a new mortgage mandate for these institutions." But this is not a residual bill. This is a sort of an emergency bill.

And as I understand the terms of the words in the bill, it does earmark for as long as the FDIC, the Bank Board, or the NCUA assistance to the institution is still outstanding at least 50 percent of its net new deposits, defined as deposits less interest and dividends credited and withdrawals, to the issuance of mortgages for one to four-family residences or co-op or condo units, to first-time home buyers at rates 1 percent over the average cost of funds for the institution's entire portfolio.

So that that is, I think, a carefully worded mandate.

Mr. **Brown**. I cannot quarrel with the wording of it. It is the effect of it with which we are concerned. We feel that it will not have a significant effect for two reasons: One, is because it is limited to the most troubled institutions, the institutions in the most serious earnings difficulties. They are not in a very strong position to make a lot of below market rate mortgage loans.

So the logic behind it is somewhat perverse, asking the weakest institutions to go out and make below market rate mortgage loans. This obviously will put them at a competitive disadvantage vis a vis other financial institutions. It will make it more difficult for them to attract deposits, and if they cannot attract deposits, why, then the trigger mechanism does not——

Mr. **St Germain**. How can you make that statement? Why is it more difficult to attract deposits if they are making loans at 1 percent over their average cost of new funds?

Mr. **Brown**. There are two answers to that. In the first place, the operating costs of savings and loans have to be added on to their cost of funds. In other words, if their cost of funds is 11 percent and their operating cost is 1.3 percent, then their true cost is 12.3 percent.

Mr. **St Germain**. How does this lower the amount of deposits they attract?

Mr. **Brown**. Because the earnings they receive on their mortgage portfolio will be less than that of other institutions which are not subject to this requirement. So they would be in a weaker position to compete for funds.

The second reason can be seen by looking at last year's data for the whole industry. The whole savings and loan industry last year had a net increase in new deposits, as defined in this bill, of negative $27 billion. In other words, the requirement would have had zero effect last year. It is not likely to have any effect this year.

And those figures are just aggregate figures for the whole industry. If you look at the position of the troubled institutions, they have an even more serious position and have a much more difficult time attracting deposits. So that the net effect of this trigger mechanism is zero under any likely scenario over the next several years. So I just do not think that the benefit is meaningful.

Chairman GONZALEZ. Well, I still think, though, that your language here fails to establish a new mortgage mandate for the institutions, perhaps needs some modification to say that in your opinion this mechanism—the bill does not fail to provide it; it provides it—but in your opinion this mechanism in reality will not have any significance at all as far as insuring participation in the mortgage market.

Mr. BROWN. I could accept that.

Chairman GONZALEZ. Well, it was just the wording. I felt it was unfair to the chairman's bill to say, "In particular it fails to establish a new mortgage mandate for these institutions," because to the extent that it can it has attempted to do that.

Now, yes, I myself this morning raised the question from the practical stark reality confronting us just how effectively we will be able to help these institutions to survive. But that is another point. It was just that that bothered me a little bit.

Thank you very much.

Mr. Schumer?

Mr. SCHUMER. I have a couple of questions, and then maybe points. I think the statement, the joint statement and the attached statements, are excellent. And it has bothered me, that if we are going to spend a lot of money to save institutions which I think need saving, there ought to be a mission and not just have them be carbon copies of the big institutions. But there ought to be some kind of mission.

Evidently before I came in the chairman issued his concern that we are a two-house body, and that if we went very far here and we might just be throwing the baby out with the bathwater. But I think overall I am very impressed with this statement and I think it adds something on the table.

I would just make one other point. It is very interesting that before 1980, I think all of Washington, Republicans and Democrats, believed in Government assistance and the New Deal, and the little people went to the Democrats and the big people, business, went for Government assistance to the Republicans. But they got it.

And what has changed is that now with Reagan, not Reaganomics, but Reagan, the Republicans cannot help. Their hands are sort of tied. They cannot help at all. So the big people as well as the little people have to come to us for help.

And I think we are missing at times those who need it and will be missing a major opportunity if we do not change things around a little bit. I think that one of the few good things about Reaganomics is that it presents an opportunity for us.

I would just like to make a couple of points. First, I think we could use a higher set aside for housing. I have no disagreement with 50 or even 100 percentage. I think maybe this should become part of the chairman's bill, which mandates that any new deposit money, a very high percentage of new deposit money, ought to go into mortgages.

I think that is a very good idea and I do not see that the two are mutually exclusive, the 50 percent overall and x percent, whatever it may be, of new money.

The second suggestion that I would make is—and we did this in New York—a variable rate mortgage. I have more trouble with the variable rate mortgage and I would like to see some more statistics on the fact that institutions could survive if interest rates go up quite a lot. I mean, the thrifts have been asked to be the shock absorber for accelerating interest rates.

I just—you state one little figure in here sort of quick, that if you had the two-thirds of wages proposal that you make, that thrifts could still survive and survive well. I would like to see a little more documentation for that.

The third thing I would say is, and this is one of the loopholes in this, there ought to be requirements that when interest rates go down the interest rate goes down as quickly as it has gone up. We have this in New York State; when we approved variable rate mortgages, we made sure that the amounts that they went up were limited. But exactly the opposite was required, too, when the interest rates went down that the mortgage rate would go down the same amount.

If that is missing you may find variable rate mortgages up, up, up and never down.

So those are just some suggestions. I would like to hear a little bit more on the variability part of the problem, which goes to the heart of the question of how thrifts can survive as distinct institutions if they cannot pass along or somehow have the cost of increasing interest rates given to somebody.

Do you have any comments on that now, or it can be later, because I am sure there is much to be done here.

Mr. **NADER**. We could supply that for the record.

[Upon Congressman Schumer's request for additional information, the following letter, dated April 20, 1982, was sent to his office from Mr. Brown:]

public interest research group
1346 connecticut ave., n.w., suite 419a
washington, d.c. 20036
(202) 833-3934

PIRG

April 20, 1982

Honorable Charles Schumer
U.S. House of Representatives
126 Cannon Building
Washington, D.C.

Dear Mr. Schumer:

When Mr. Nader and I testified before the Housing Subcommittee on March 18, 1982 concerning H.R. 5568, you requested further information on the earnings flexibility of savings institutions if their adjustable rate mortgages (ARMs) were subject to the payment and loan balance increase limits that we proposed. The enclosed memo entitled *Borrower Safeguards on Adjustable Rate Mortgages* (June 15, 1981) provides an analysis of ARM rate flexibility under constraints very similar to those we proposed in our testimony. Chart VII in the memo shows the maximum interest rate adjustments permitted under two different payment increase limits -- a 2/3 wage increase limit, and a full wage increase limit. The Chart VII analysis does not use negative amortization.

Chart VIII of the memo shows the maximum interest rate increases permitted if payment increases are limited to 2/3 the wage rate and loan balance increases are limited to 1/5 the inflation rate. As can be seen, allowing some negative amortization provides much greater short run interest rate flexibility. Given the wage and inflation rates of recent years the interest rate can increase by as much as 3% in one year and 4% over a two year period.

The constraints used in Chart VIII are not quite as restrictive as those proposed in our testimony, which would limit loan balance increases by the lesser of the inflation rate or home appreciation rate. Also enclosed is a set of simulations entitled *Adjustable Rate Mortgages Simulations* (May, 1981). These simulations provide an extended analysis of the payment and loan balance increase limits used in Chart VIII of the memo.

We have also calculated the interest rate increases that would have occurred in recent years on an ARM that used the FHLBB's conventional mortgage rate series as its rate adjustment index and limited payment increases by the full wage rate and loan balance increases by the inflation rate or home appreciation rate, whichever is less. An ARM made in January, 1974 at 8.64% would have had an interest rate of 15.1% as of January, 1982. An ARM made in January, 1979 at 10.33% would have had an interest rate of 14.6% as of January, 1982. Given the wage increase, price increase, and home appreciation rates for 1981, an ARM made in January, 1981 at 14% could have had its interest rate raised to 16.4% on January, 1982, if its rate adjustment index had risen enough to justify a 2.4% rate increase.

We greatly appreciate your interest in the vital issue of safe and sound mortgage instruments. If we can provide you with additional information please let us know.

Sincerely,

Jonathan Brown
Jonathan Brown

public interest research group
1346 connecticut ave., n.w., suite 419a
washington, d.c. 20036
(202) 833-3934

PIRG

Borrower Safeguards on Adjustable Rate Mortgages: Evaluation of Alternative Limits on Interest Rate and Monthly Payment Increases

June 15, 1981

The most critical issue in developing statutory safeguards for adjustable rate mortgages (ARMs) is how to best limit yearly interest rate and monthly payment increases. One approach is to impose a direct limit on interest rate increases per year; another is to impose a direct limit on monthly payment increases. This choice is compounded by a collateral issue, negative amortization. If negative amortization is prohibited, the issue is simply whether to impose a direct limit on interest rate or payment increases. If negative amortization is permitted, there should be a direct limit on payment increases and another direct limit on loan balance increases. In this case the issue is whether to impose an additional, direct limit on interest rate increases.

I. ARMs Without Negative Amortization

A. Goal of Interest Rate or Payment Increase Limits

If negative amortization is prohibited, a limit on the maximum interest rate increase per year and a limit on the maximum monthly payment increase per year have the same basic purpose - to restrain payment increases so that they do not rise faster than borrower income in periods of sharp interest rate escalation. The interest rate increase limit serves an additional purpose - to restrain negative amortization - if negative amortization is permitted.

When negative amortization is prohibited, a direct limit on interest rate increases indirectly sets a limit on monthly payment increases and, conversely, a direct limit on payment increases indirectly sets a limit on interest rate increases. Since either type of limit can restrain payment increases - one directly, the other indirectly - the one that does this most efficiently should be chosen. Having both an interest rate and a payment limit would be unnecessary, unless it can be shown that the two limits in combination are the best way to restrain payment increases.

Selecting the best interest rate or payment limit first requires an understanding of the relationship between interest rates and the growth rate of borrower income. For the purpose of ARM safeguards, the best measure of borrower income growth is the wage increase rate. Wage data is available on a current basis from the Bureau of Labor Statistics, while there are considerable time lags involved in the publication of other indices, such as median family income. The wage increase rate can be viewed as either the rate of increase of the average wage of U.S. workers or the average rate of increase of U.S. workers' wages, since these two measures are equivalent. The wage increase rate is loosely linked to interest rates by means of the inflation rate. When inflation accelerates, the wage increase rate rises, although often with a significant lag, and interest rates also rise. Chart I below provides a historical comparison of the mortgage rate, the rate of increase of the Consumer Price Index, and the rate of increase of the average wage of U.S. workers. The wage increase rates are derived from the Bureau of Labor Statistics' series for the average weekly earnings of production or nonsupervisory workers on private non-farm payrolls.

CHART I - Historical Data on Interest Rates, Inflation, and Wages

Year	Mortgage[1] Rate	CPI[2] Increase Rate	Wage[3] Increase Rate
1965	5.95%	1.9%	3.9%
1966	6.41	3.4	2.9
1967	6.52	3.0	3.6
1968	7.03	4.7	6.8
1969	7.82	6.1	6.2
1970	8.36	5.5	4.1
1971	7.67	3.4	7.8
1972	7.51	3.4	6.5
1973	8.01	8.8	6.6
1974	9.01	12.2	6.6
1975	9.21	7.0	6.7
1976	9.11	4.8	6.8

Year	Mortgage Rate	CPI Increase Rate	Wage Increase Rate
1977	9.02	6.8	7.4
1978	9.58	9.0	9.1
1979	10.92	13.3	7.4
1980	12.95	12.4	7.9
1981	14.64 (May)	9.6 (1st Q)	-

[1] Yearly Average - FHLBB Series-Effective Rate - Existing Homes
[2] December to December - BLS Series
[3] December to December - BLS Series

The historical data suggest that the mortgage rate will tend to be 2% to 4% above the inflation rate. However, a sharp acceleration of inflation that is not expected to continue can temporarily drive the CPI rate above the mortgage rate. Also, a prolonged period of monetary restraint may drive the mortgage rate far above the inflation rate - a situation which seems to be developing in 1981.

The historical data also suggest that the wage increase rate is likely to be roughly equal to or slightly above the inflation rate at low inflation rates and yet lag significantly behind the inflation rate at high inflation rates. This primarily reflects the fact that wage increase rates are sluggish in the face of accelerating inflation. The wage increase rate will be closer to the inflation rate at high inflation rates if the high inflation rate has been sustained for a number of years. Also, when the inflation rate falls sharply, the wage increase rate temporarily may remain above it, as occurred in 1976.

Given the variability in the wage increase rate - inflation rate relationship and the inflation rate - mortgage rate relationship, there clearly is no single wage increase rate associated with each mortgage rate. However, it is possible to estimate a probable range of wage increase rates for each mortgage rate. Chart II below provides such estimates. For each mortgage rate the high wage increase rate represents the rate that would be likely if the inflation rate had been stable for several years, the wage increase rate had fully adjusted to the inflation rate, and the mortgage rate maintained a normal spread above the inflation rate. The low wage increase rate represents the rate that would be likely if inflation had accelerated sharply for several years with the wage increase rate lagging behind and expectations of continuing high inflation or restrictive monetary policy had raised the mortgage rate to its normal spread above the inflation rate. In both cases the mortgage rate is assumed to be 3% above the inflation rate. Situations in which the inflation rate and interest rates decline are not considered, since declining mortgage rate situations are not germaine to limits on ARM interest rate or payment increases. It is also important to remember that the estimated relationship between the mortgage rate and the wage increase rate would not hold if a short term rate, such as the 3 month Treasury bill rate, were used instead of the mortgage rate. Short term interest rates are very volatile and cyclical changes in the short term rate could easily override the trend relationship between interest rates and wage increase rates.

CHART II - Estimated Wage Increase Rates

Mortgage Rate	High Wage Increase Rate	Low Wage Increase Rate	Average Wage Increase Rate	2/3 Average Increase Rate
6%	5%	2%	3.5%	2.4%
8	7	4	5.5	3.7
10	8	5	6.5	4.4
12	10	6	8.0	5.4
14	11	7	9.0	6.0
16	12	8	10.0	6.7
18	14	9	11.5	7.7
20	15	10	12.5	8.4

The historical data and estimates indicate that on average the wage increase rate will rise as the mortgage rate rises. This has crucial significance for limits on ARM rate or payment increases. When the wage increase rate is higher, borrowers should be able to manage higher percentage increases in mortgage payments. For example, if wages increase at a 4% annual rate, then a 4% annual increase in mortgage payments will result in the share of a borrower's wage income allocated to mortgage payments remaining constant. If the wage increase rate is 10%, payments can increase at a 10% rate and the mortgage payment share of wage income will still remain the same.

The goal of an ARM limit is not to constrain all mortgage payment increases as much as possible, but rather to make sure that mortgage payments do not increase at a faster rate than borrower income. Since wage increase rates are higher at higher mortgage rates, an efficient limit should permit higher payment increase rates at higher mortgage rates. A limit that permitted mortgage payments to increase at a higher rate at lower mortgage rates would be at cross purposes with borrowers' wage income experience. Even a uniform payment increase rate limit - say, 7% - applicable at all mortgage rates would be inefficient, since it would underprotect borrowers at low mortgage rate levels and overprotect borrowers at high mortgage rate levels.

An efficient limit on interest rate or payment increases should permit the payment increase rate to shift upward in a manner similar to the estimated wage increase rates shown in Chart II. However, one important qualification must attach to the use of estimated wage increase rates as targets for payment increase rates. The data on wage increases refers to the average rate of increase of U.S. workers' wages. By definition, the wage increase rate for many workers is below the average wage increase rate. Thus, it would be wise to use some fraction, probably 2/3, of the average wage increase rate as the target for payment increase rates.

The estimated wage increase rates shown in Chart II, reduced by 1/3, provide a reasonable schedule of target payment increase rates. These target rates for payment increases are shown in Chart III. Any proposed limit on ARM interest rate or payment increases should be judged by how close the payment increase rates that it generates come to the target rates.

CHART III - Target Payment Increase Rates (2/3 Estimated Wage Increase Rates

Mortgage Rate	High	Low	Average
6	3.4%	1.3%	2.4%
8	4.7	2.7	3.7
10	5.4	3.4	4.4
12	6.7	4.0	5.4
14	7.4	4.7	6.0
16	8.0	5.4	6.7
18	9.4	6.0	7.7
20	10.0	6.7	8.4

B. Fixed Interest Rate Increase Limit

One approach to ARM safeguards is to limit interest rate increases per year by some fixed amount, for example, 1/2% per year. Prior to abandoning all limits on interest rate increases in April of this year, the FHLBB had imposed such a 1/2% limit on VRMs and ARMs made by federal S&Ls. The primary consequence of a fixed limit is the downward shift in the payment increase rate as the mortgage rate rises. This occurs because the monthly payment is much greater at high mortgage rate levels than at low levels, while the increase in the monthly payment resulting from a fixed interest rate increase is relatively constant at all mortgage rate levels. With growing payment levels but relatively constant payment increases, a given interest rate increase will generate a lower percentage change in payments - i.e., low payment increase rate - the higher the mortgage rate level. For example, with a 30 year, $50,000 mortgage the initial monthly payment is $300 at a 6% interest rate but $754 at 18%. However, the monthly payment increase generated by a 1/2% interest rate increase only rises from $15.90 at 6% to $20.35 at 18%. The 1/2% interest rate increase results in a 5.3% payment increase if the mortgage rate is 6%, but only a 2.7% payment increase if the mortgage rate is 18%.

Chart IV below shows the payment increase rate generated by a 1/2% interest rate increase and a 2% interest rate increase at a different mortgage rates levels. The calculations assume that mortgage term = 30 years and that the rate adjustment occurs at the beginning of the second year.

CHART IV - Payment Increase Rates for Fixed Interest Rate
Increase Limits

Mortgage Rate	1/2% Per Year	2% Per Year	Target Payment Increase Rate[1]
6%	5.3%	21.9%	2.4%
8	4.7	19.3	3.7
10	4.2	17.0	4.4
12	3.7	15.0	5.4
14	3.3	13.4	6.0
16	3.0	12.0	6.7
18	2.7	10.8	7.7
20	2.5	9.9	8.4

[1] Chart III

It should be noted that the payment increase generated by a given interest rate increase at a given mortgage rate level will vary depending on the age of the mortgage. As stated above, Chart IV assumes that the interest rate adjustment occurs at the start of the second year. If the adjustment were to occur in a later year, the payment increase and the payment increase rate would be less. For example, with an initial mortgage rate of 9% a 1/2% interest rate increase will cause payments to increase by 4.43% if it occurs at the start of the 2nd year, by 3.60% if it occurs at the start of the 11th year, and by 2.95% if it occurs at the start of the 16th year. However, from the perspective of devising ARM limits, the greater payment increase rates in the early years of the mortgage are the most relevant.

Chart IV demonstrates clearly that a fixed interest rate increase limit is an inefficient type of limit. Even a very strict limit of 1/2% per year cannot prevent payments from increasing at a faster rate than wages at low mortgage rate levels. On the other hand, at high interest rate levels a 1/2% limit would constrain the payment increase rate far below the wage increase rate.

Advocating a fixed interest rate increase limit is a poor strategy for protecting borrowers. A case could be made that a 1/2% limit would hold payment increase rates to tolerable levels - somewhat above wage increase rates - at low mortgage rates, while providing very strong protection - actually, overkill - at high mortgage rates. But in today's financial and political climate, it may be unrealistic to think that a 1/2% limit could be enacted into law. It is possible that the most restrictive fixed interest rate increase limit that could be obtained would be 2% per year. The grave danger with advancing a 1/2% limit as an initial bargaining position is that the concept of a fixed limit will be accepted but the limit raised to a much higher level. A high limit would allow exorbitant payment increase rates at low mortgage rate levels which would cause extreme financial hardship for many borrowers. For example, with a 2% per year limit and an initial mortgage rate of 6%, payments could increase 21.9% in one year while it would be unlikely for wages to increase at a rate much above 3% per year.

C. Ratio Interest Rate Increase Limit Tied to Mortgage Rate

A second approach is to limit interest rate increases to a fraction - perhaps 1/10 - of the prevailing mortgage rate at the time of adjustment. For example, with a 1/10 ratio limit, if the interest rate on new mortgage originations were 15%, then the maximum interest rate adjustment for all outstanding ARMs would be 1.5%. This ratio approach would permit larger interest rate increases at higher mortgage rate levels. The larger interest rate increases would in turn allow for a modest increase in the payment increase rate as the mortgage rate level rises. Chart IV below shows the payment increase rates generated by a 1/10 ratio limit and a 1/20 ratio limit.

CHART V - Payment Increase Rates for Ratio Interest Rate Increase Limits Tied to Mortgage Rate

Mortgage Rate	1/20 Ratio Limit	1/10 Ratio Limit	Target Payment Increase Rate[1]
6%	3.2%	6.4%	2.4%
8	3.8	7.6	3.7
10	4.2	8.4	4.4
12	4.5	9.0	5.4
14	4.7	9.4	6.0
16	4.8	9.6	6.7
18	4.9	9.8	7.7
20	4.9	9.9	8.4

[1] Chart III

As shown by Chart V, a ratio limit generates a payment increase schedule that is a great improvement over the downward shifting schedule generated by a fixed limit. However, the payment increase schedule is still relatively flat - little upward shifting at high mortgage rate levels - and thus still somewhat inefficient. The payment increase rate must be held unnecessarily low at high mortgage rate levels, if it is to be kept below likely wage increase rates at low mortgage rate levels. A 1/20 ratio limit would provide reasonably good borrower protection at low mortgage rate levels. But a 1/20 ratio limit, which would limit interest rate increases to 0.7% per year when mortgage rates were 14%, would be viewed by lenders as very restrictive and would be difficult to enact into law. Bargaining that led to a more liberal ratio limit, for example, a 1/10 ratio limit, would establish a limit that clearly could not hold the payment increase rate below the wage increase rate at low mortgage rate levels. The more liberal the ratio limit, the greater its failure to protect borrowers at low mortgage rate levels.

D. Ratio Interest Rate Increase Limit Tied to Inflation Rate

A third approach is to limit interest rate increases to 1/10 of the inflation rate. This approach generates a schedule of payment increase rates that shifts upward in similar fashion to the schedule of estimated wage increase rates. As shown in Chart VI below, the payment increase rates generated by this limit are slightly below the full estimated wage increase rates but slightly above 2/3 of the estimated wage increase rates (the target payment increase rates in Chart III).

CHART VI - Payment Increase Rates with Interest Rate Increases Limited to 1/10 the Inflation Rate

Mortgage Rate	Inflation Rate	1/10 Inflation Rate	Payment Increase Rate	2/3 Estimated Wage Increase Rate	Est. Wage Increase Rate
6%	3%	.3	3.2	2.4	3.5
8	5	.5	4.7	3.7	5.5
10	7	.7	5.9	4.4	6.5
12	9	.9	6.7	5.4	8.0
14	11	1.1	7.3	6.0	9.0
16	13	1.3	7.8	6.7	10.0
18	15	1.5	8.1	7.7	11.5
20	17	1.7	8.4	8.4	12.5

While a limit of 1/10 the inflation rate appears to be relatively efficient in terms of matching payment increase rates with expected wage increase rates, it has a serious drawback. Chart VI assumes a constant 3% spread between the inflation rate and the mortgage rate. While a constant spread may accurately describe the historical trend, it certainly does not reflect the actural spread on a year to year basis. The inflation rate, at least as measured by the CPI, is far more volatile than the wage increase rate or the mortgage rate. When inflation accelerates sharply, the inflation rate can even rise above the mortgage rate, as occurred in 1973-74 and 1979. In such situations the wage increase rate will most likely lag far behind the inflation rate. Tying the payment increase rate to the inflation rate could result in payment increase rates far in excess of the wage increase rate. For example, the 1/10 limit applied to the 12.2% inflation rate for 1974 would have permitted an interest rate increase of 1.2% at the beginning of 1975. With a 9% mortgage adjusted at the end of the first year, this would represent a 10.7% payment increase, yet in 1975 the average wage increase rate was only 6.7%. Although the ratio limit maintains a good relationship between trend payment increases and trend wage increases, it does not do a good job of protecting borrowers on a year to year basis.

A ratio limit tied to the mortgage rate, as discussed in the previous section, suffers from the same drawback as a ratio limit tied to the inflation rate, although not to the same extent since the mortgage rate is not as volatile as the inflation rate. In a year of sharp mortgage rate increases a mortgage rate based ratio limit would most likely generate a payment increase rate that is much greater than the actual wage increase rate. This drawback would be greatly aggravated if ARMs became widespread. If ARMs replace fixed rate mortgages as the standard mortgage instrument, the mortgage origination rate will acquire some of the characteristics of short or intermediate term interest rate and this will increase its volatility. The more volatile the interest rate to which the ratio limit is applied, the weaker the borrower safeguard provided by the limit.

E. Direct Payment Increase Limit

A fourth approach is to impose a direct limit on payment increases, rather than limit them indirectly by an interest rate increase limit. The most suitable limit for the payment increase rate would be 2/3 the wage increase rate of the preceding year. This limit would reflect the actual wage increase rate, rather than the target payment increase rates used in the previous analysis, which are merely estimates of trend wage increase rates.

If negative amortization is prohibited, then a direct payment increase limit also sets an indirect limit on interest rate increases. Chart VII below shows the range of probable indirect interest rate increase limits associated with two alternative wage based payment increase limits. In one case the payment increase rate is limited to 2/3 the wage increase rate, while in the other it is limited to the full wage increase rate. Obviously, there are many possible wage increase rates that could occur at each mortgage rate level. The exact payment increase limit cannot be determined until the wage increase rate for the preceding year is known. To estimate the interest rate increase limits the set of high, low, and average estimated wage increase rates shown in Chart II is used again. The payment increase limits associated with these wage increase rates are transformed into a range of probable interest rate increase limits for each mortgage rate.

As indicated in a previous section, for any given mortgage rate and interest rate increase, the payment increase rate will be smaller the older the age of the mortgage. Conversely, a given mortgage rate and payment increase rate will result in a larger interest rate increase the older the mortgage. Chart VII assumes that the rate adjustments come at the start of the 2nd year. If the adjustments were to come later, the numbers shown would be slightly larger. For example, with a 10% mortgage rate and payment limit set at 2/3 the wage increase rate, if the adjustment were to come at the start of the 11th year instead of the 2nd year, the average interest rate increase limit would be 0.6% instead of 0.5%.

CHART VII - Indirect Interest Rate Increase Limits Generated By Wage Based Payment Increase Limits

Mortgage Rate	Payment Limit at 2/3 Wage Increase Rate (WIR)			Payment Limit at Full Wage Increase Rate (WIR)		
	Avg. WIR	High WIR	Low WIR	Avg. WIR	High WIR	Low WIR
6%	.22%	.32%	.13	.33%	.47%	.19%
8	.39	.50	.29	.58	.74	.43
10	.52	.64	.40	.78	.95	.60
12	.72	.90	.54	1.07	1.34	.81
14	.91	1.11	.71	1.35	1.65	1.05
16	1.12	1.34	.90	1.67	2.00	1.34
18	1.42	1.73	1.11	2.12	2.58	1.66
20	1.70	2.03	1.36	2.54	3.04	2.03

A wage based direct limit on payment increases accomplishes the basic goal of making sure that payments do not increase faster than wage income. Since it is always on target, it is clearly more efficient than direct limits on interest rate increases. A direct payment increase limit does not result in a misshaped payment increase rate schedule that underprotects borrowers at low mortgage rate levels and overprotects them at high rate levels. Moreover, it will automatically adjust to protect borrowers when wage increase rates are abnormally sluggish. Even a direct interest rate increase limit that successfully approximates the historical trend relationship between mortgage rates and wage increase rates cannot accomplish this.

The efficiency inherent in the wage based payment limit is particularly important given the bargaining process that will shape any statutory limit. Obviously, lenders will seek to weaken as much as possible any limit that is proposed. A wage based payment limit is still efficient even though it is raised from 2/3 the wage increase rate to the full wage increase rate. On the other hand, raising the various direct limits on interest rate increases magnifies their inefficiencies and greatly increases the likelihood of payments increasing much faster than wages at low mortgage rate levels or whenever wages are unusually sluggish.

Another possibility that merits consideration is imposing both a direct payment increase limit and a direct interest rate increase limit. Whichever limit was more restrictive in any given situation would be binding. For example, a payment increase rate limit equal to the wage increase rate could be combined with a 2% limit on interest rate increases per year. As shown in Chart VII, this payment increase limit would in most cases constrain interest rate increases to less than 2% at mortgage rate levels below 18%. At mortgage rates above 18%, the 2% interest rate increase limit would in most cases constrain the payment increase rate to less than the wage increase rate. The drawback with this approach is that there is no evidence that suggests that borrowers are less able to afford payment increase rates equal to the full wage increase rate at high wage increase rate levels than at low wage increase rate levels. This would be true for borrowers with fixed incomes, but ARMs - at least those that are likely to exist in today's financial environment - are probably not a good mortgage for such borrowers. The best strategy for protecting fixed income borrowers is to maintain a supply of fixed rate mortgages. As for the vast majority of borrowers, who do have rising incomes, without evidence that the distribution of wage increase rates becomes more disperse at high wage increase rate levels, there is no borrower benefit in creating a more protective standard for high wage increase rate levels by coupling an interest rate increase limit to a wage based payment increase limit. More important, the lending industry would undoubtedly use the addition of an interest rate increase limit, especially one set at a relatively low rate, as an argument for weakening the wage based payment increase limit. This would be a very poor trade-off from the borrower's perspective.

Finally, it is important to recognize that there is a powerful political advantage in advocating a wage based payment increase limit instead of a direct interest rate increase limit. Given the present financial environment, lenders, particularly S&Ls, often have a receptive audience in Congress, state legislatures, and the media when they claim that they need greater interest rate flexibility on mortgages. It will be much more difficult for lenders to find a favorable response if they have to argue that mortgage payments should be allowed to increase faster than borrowers' wage income.

II. ARMs With Negative Amortization

A. Utility of Negative Amortization

For ARMs without negative amortization, any interest rate increase and the accompanying payment increase must always be equivalent. If there are separate limits for interest rate increases, and payment increases, whichever limit is the most restrictive will limit both the interest rate increase and the payment increase. This equivalence of limits occurs because without negative amortization an interest rate increase must be fully reflected in the payment increase and a payment increase can only be generated by an interest rate increase.

The automatic equivalence of limits is broken once negative amortization is permitted. Negative amortization (an increase in the loan balance) takes place whenever an interest rate increase is accompanied by a payment increase that is smaller than the payment increase normally associated with the interest rate increase.* In the absence of negative amortization the payment increase must cover the increased interest charge associated with the higher interest rate. With negative amortization the payment increase is not large enough to cover the increased interest charge. This part of the interest charge is added to the loan balance.

However, the loan balance may not increase by the full amount of the interest charge increase less the payment increase. Normally a portion of mortgage payments goes to reduce the loan balance, although this portion is very small in the early years of a mortgage. Thus, when a payment shortfall occurs, this payment portion, rather than reduce the loan balance, will be applied to the uncovered interest charge. Thus, the loan balance will increase by an amount equal to the uncovered interest charge less this payment portion.

Negative amortization is possible under a variety of limits on payment, loan balance, and interest rate increases. Even where the interest rate and the payment increase limits are equivalent - a situation that normally implies no negative amortization -

---

*Strictly speaking, as defined here, negative amortization includes not only the case of a loan balance increase, but also the situation in which the loan balance declines but the payment, if maintained for the remaining term of the mortgage, is not large enough to reduce the loan balance to zero by the end of the term.

negative amortization could still occur if a lender voluntarily adopted a payment increase limit that was more restrictive than the mandatory payment increase limit. However, if the mandatory payment limit is strict, it is unlikely that a lender would voluntarily adopt an even more restrictive limit. Thus, such "voluntary" negative amortization would be rare. On the other hand, where the mandatory payment increase limit is below the interest rate increase limit, lenders will not be able to take full advantage of the higher interest rate limit, unless they use negative amortization.

Since adoption of a strict payment limit and a more liberal interest rate limit would exert strong pressure on lenders to use negative amortization, it is important to ask whether it is generally in borrowers' interest to encourage widespread use of negative amortization. Negative amortization is useful because it permits imposition of a strict payment increase limit - say, 2/3 of the wage increase rate - and, yet, still provides lenders with considerable short term interest rate flexibility. With the phase out of Regulation Q in progress lenders are seeking interest rate flexibility on their loans to match greater interest rate volatility on their deposits. Permitting some negative amortization to improve interest rate flexibility will make it easier to enact into law a strict payment increase limit. This trade-off seems worthwhile from the borrower's perspective. It would prevent payments from rising too fast in periods of interest rate escalation and yet allow them to rise to higher levels when interest rates began to moderate. This will significantly reduce payment volatility, the greatest borrower concern with ARMs. Of course, payments may be higher in the subsequent years because of larger loan balances. But taking inflation into consideration, the additional payments will not be greater, in real terms, than the payment savings in the previous years.

However, it is essential to adopt a strict direct limit on negative amortization in order to make it very unlikely that a borrower's loan balance could increase faster than the value of his or her home. Were the loan balance permitted to grow faster than the home appreciation rate, the home owner's equity would be eroded, a very unsound situation. A possible direct limit on loan balance increases per year would be the lesser of 1/5 the inflation rate for the previous year or 1/5 the rate of increase in the average sales price of existing homes in the U.S. for the previous year.

B. Indirect Interest Rate Increase Limit Derived from the Payment Increase and Loan Balance Increase Limits

The most complex issue raised by negative amortization is what type of limit should be set for interest rate increases once strict limits have been imposed on payment and loan balance increases. In selecting an interest rate increase limit is is important to recognize that, even in the absence of a direct interest rate limit, the payment and loan balance limits will in concert indirectly limit interest rate increases. However, this indirect, derived interest rate increase limit cannot be specified once specific payment and loan balance limits are given. The indirect, derived limit will vary considerably from year to year depending on the wage increase rate, the inflation rate, and, if negative amortization has occurred, the loan balance increase rate for the preceding year. A higher wage increase rate or inflation rate for the preceding year will allow a greater payment increase or loan balance increase in the present year which in turn will allow for a greater interest rate increase. On the other hand, if negative amortization has been high in the preceding year - in particular, close to the loan balance increase limit - the indirect, derived interest rate increase limit will be much lower than it would have been if negative amortization had been lower in the preceding year. In simplified terms, this happens because a relatively large loan balance increase in one year will in large part be repeated in the next year even though the interest rate has not increased. For example, if payments in one year are so short of the interest charge that a 2% increase in the loan balance occurs, in the next year, even though the interest rate does not change and the payments are increased somewhat to reflect the wage increase rate, the payment shortfall will be almost as great as in the first year and the loan balance will grow by almost 2%.

The indirect, derived interest rate increase limit will also vary depending on the age of the mortgage. The older the mortgage, the greater the interest rate increase generated by a given payment increase and loan balance increase. This occurs because the older the mortgage, the greater the portion of payments used to reduce the loan balance as opposed to covering the interest charge. As mentioned above, when there is a payment shortfall, the loan balance will not increase unless the uncovered interest charge is greater than the payment portion that was used to reduce the loan balance in the previous period.* The larger the payment portion for loan balance reduction, the greater the ability to offset the uncovered interest charge without resorting to increasing the loan balance. Hence, the older the mortgage, the greater the potential to absorb large interest rate increases without generating loan balance increases that exceed the loan balance increase limit.

Chart VIII below gives an example of the maximum interest rate increase that could occur early in the life of a mortgage with a payment limit of 2/3 the wage increase rate and a loan balance limit of 1/5 the inflation rate. The initial mortgage rate is set at 9.15%, the mortgage rate for the month of January 1978. The maximum mortgage rate for each succeeding year represents the highest rate permitted by the payment and loan balance limits, given the wage increase and inflation rates for the previous year. The Chart also shows the original mortgage rate adjusted according to two different indexes. The index adjusted mortgage rate shows the mortgage rate increases that could occur if there were no limits of any kind. Adjustments with the long term rate index are based on changes in the rate on fixed rate mortgages, while the short term rate index uses changes in the rate on 6 month Treasury bills. The index values used were the average index interest rate for the month of January for the years 1978 through 1981. The wage increase rate and inflation rate values reflect historical data for the years 1978-80; for 1981 and 1982 the values are merely projections.

---

*Technically, the appropriate measure is the payment portion that would have been used to reduce the loan balance in the current period if the interest rate had not been increased.

CHART VIII - Maximum Interest Rate Increase Permitted With Strict Payment and Loan Balance Limits

Year	Maximum Mortgage Rate	Mortgage Rate: Long Term Rate Index	Mortgage Rate: Short Term Rate Index	CPI Increase Rate	Wage Increase Rate
1978	9.15%	9.15%	9.15%	9.0%	5.9%
1979	12.10	10.33	12.11	13.3	7.4
1980	13.3	12.10	14.59	12.4	8.2
1981	13.4	13.67	17.39	10.0	9.0
1982	13.3	-	-	10.0	9.0
1983	13.7	-	-	-	-

Chart VIII shows that in the early years of the mortgage the payment and loan balance limits would limit interest rate increases to roughly 3% in a single year and cumulatively 4% or 5% over a five year period. Lower wage increase and inflation rates would result in a lower indirect, derived limit on interest rate increases, while high wage increase and inflation rates would raise this limit.

Chart IX below shows the maximum interest rate increase that could take place in the 20th year of the mortgage, instead of the 1st year as in the Chart VIII case. The payment and loan balance limits used in the Chart VIII case are also used in the Chart IX case. The example assumes a mortgage that has an interest rate of 15% during the 19th year and a loan balance of $48,964 at the end of the 19th year. This implies that some negative amortization has occurred during the early years of the mortgage. However, the example assumes that payments during the 19th year were sufficient to amortize the loan over its remaining term. An ARM simulation that generates this mortgage pattern is provided by Simulation II of PIRG's Preliminary Proposal For a Federal Statute To Protect Mortgage Borrowers, May 1981.

CHART IX - Maximum Interest Rate Increase Permitted on an Older Mortgage

Mortgage Year	Maximum Mortgage Rate	Loan Balance (End of Year)	CPI Increase Rate	Wage Increase Rate
19	15% (stable)	$48,964	10%	11%
20	22.6	49,943	13	10
21	24.1	51,242	10	10
22	24.4	52,267	--	--

Chart IX shows that with wage increase rates and inflation rates roughly similar to those in Chart VIII in the 20th year of a mortgage the interest rate could jump from 15% to 22.6%, an increase of 7.6%, as opposed to the 2.95% maximum interest rate increase shown in Chart VIII when the rate increase occurs in the first year of the mortgage. After this large initial jump, the interest rate increases in subsequent years are far more moderate.

The two charts indicate that strict payment and loan balance limits without any direct interest rate limit will give lenders great interest rate flexibility over a 1 or 2 year period. On the other hand, such limits would prevent large interest rate increases - say, 2% per year or more - in successive years for a longer period. Thus, the payment and loan balance limits will preclude any prolonged sharp increases in the interest rate.

However, large interest rate increases during the last 10 years of the mortgage present a special problem. Such interest rate jumps may make it impossible to amortize the mortgage over its original term (reduce the loan balance to zero). One solution to this problem would be to prohibit negative amortization during the last 10 years of the mortgage. Prohibiting negative amortization in this context would not just rule out loan balance increases but would make sure that the loan balance continued to decline. In other words the payment portion that goes to reduce the loan balance could not be used to cover increased interest charges. This would reduce interest rate flexibility on old mortgages, but should not be onerous for lenders, since mortgages over 20 years old constitute only a very small portion of their total mortgage loan portfolios.

BEST DOCUMENT AVAILABLE

C. Direct Interest Rate Increase Limit in Addition to the Payment Increase and Loan Balance Increase Limits

In evaluating the merits of a direct limit on interest rate increases, in addition to payment and loan balance limits, the key question is under what circumstances would a direct limit restrain interest rate increases more than the indirect limit derived from the payment and loan balance limits. If the direct limit were very restrictive, it could constrain payment increases more than the payment increase limit. This would also preclude negative amortization. In this case, the direct limit would restrict interest rate increases far more than the indirect, derived limit. If the direct limit were somewhat less restrictive, it could allow the payment to increase to the full payment limit and permit some negative amortization, but less negative amortization than that permitted by the loan balance limit. In this case, the direct limit could in some circumstances restrict interest rate increases more than the indirect, derived limit.

A direct interest rate increase limit of 1/2% per year would constrain payment increases more than a payment increase limit set at 2/3 the wage increase rate, except at low mortgage rate levels. Thus, at current mortgage rate levels, the direct 1/2% per year limit would restrict interest rate increases more than the payment increase limit. According to Chart VII a payment increase limit set at 2/3 the wage increase rate would on average allow interest rate increases in excess of 1/2% per year, except for mortgage rate levels below 10%. A somewhat less restrictive direct interest rate increase limit of 1% per year would still constrain payment and interest rate increases more than the payment increase limit at mortgage rate levels of roughly 15% and above. A more liberal direct interest rate increase limit of 2% per year would only constrain payment increase more than the payment increase limit at mortgage rates in excess of 20%.

A direct interest rate increase limit of 1/2% per year would eliminate the interest rate flexibility otherwise provided by the payment and loan balance limits. A 1% per year limit, while not restricting payment increases more than the payment limit, unless the mortgage rate is 15% or more, would still greatly reduce the interest rate flexibility provided by negative amortization. With a direct limit of 1% per year, it would take four years to raise the mortgage rate 4% (400 basis points). In the absence of such a direct limit, the indirect limit derived from the payment and loan balance limits would permit the mortgage rate to be raised 3% or 4% in a single year early in the life of the mortgage and somewhat more later in the life of the mortgage.

Even a direct interest rate limit of 2% per year could impose some constraint on interest rate flexibility. Such constraint is likely to be modest for ARMs that use a relatively stable, long term rate index, such as the rate on the standard, 30 year fixed rate mortgage. Based on historical experience an index based on the mortgage rate is not likely to increase much more than 2% per year. Thus, even though the indirect, derived interest rate increase limit could permit a 3% or 4% rate jump in a single year early in the life of a mortgage and a 7% or 8% jump in a single year in the last 10 years of the mortgage, it would require highly unusual economic circumstances before an index based on the mortgage rate would jump by such an amount in a single year. However, if ARMs replace fixed rate mortgages as the standard mortgage instrument, the mortgage rate and any index based on it will most likely become more volatile than in the past.

A 2% per year limit would be more likely to constrain an ARM using a volatile, short term interest rate for an index. Such an index could easily rise 7% or 8% (700 or 800 basis points) in a single year. Thus, in the absence of a direct 2% per year limit, the index could trigger a rate adjustments in the full amount of the indirect interest rate increase limit. As indicated above, large interest rate jumps toward the end of the mortgage could be eliminated by prohibiting negative amortization in the last 10 years of the mortgage. This would still leave open the question of whether a 2% per year limit - or a 1% per year limit - is needed to preclude an interest rate jump of 3% or 4% in a single year early in the life of the mortgage.

The primary borrower benefit from a direct, 2% limit would be that it would take lenders 2 years rather than 1 year to implement a 4% interest rate increase. Thus, it could dampen the interest rate jump in a single year. However, the issue is more complex. When the rate adjustment index has increased in successive years for 3 years or more, the indirect, derived interest rate increase limit will be more constraining than a 2% per year limit. As shown by Chart VIII, once a large upward rate adjustment of say 4% has occurred, the indirect, derived interest rate limit will permit only small interest rate increases - generally less than 1/2% per year - in the succeeding years. Thus, the net gain in borrower protection from a 2% per year limit would be the ability to constrain the interest rate increase in several single years over the life of the mortgage and these single years would have to be spaced at least 4 or 5 years apart. In any single year in which the direct 2% per year limit did constrain the interest rate increase, the amount of negative amortization would be less than it would have been without the 2% limit and this would mean slightly lower payments in future years.

However, if a direct interest rate increase limit is established, even one as liberal as 2% per year, this could well come about as part of a legislative trade-off that allowed a more liberal limit on payment increases. In this case, ARM borrowers would have to accept faster payment increases in periods of rapid interest rate acceleration - the effect of a more liberal payment limit - in return for slower payment increases when interest rates were moderating - the effect of less negative amortization due to constraint from the 2% per year limit. Such lincreased payment volatility does not seem a good bargain for borrowers.

Even more important, the more liberal payment limit that could result from a trade-off would weaken the indirect, derived interest rate increase limit. A weaker, indirect, derived limit would permit greater, successive interest rate increases in the years following a sharp single or two year jump in the interest rate. Since the indirect, derived limit constrains interest rate increases more in these years than the direct limit, the trade-off would result in less borrower protection against sustained interest rate increases. For example, if an ARM interest rate has risen 4% over two years, strict payment and loan balance limits are likely to hold any interest rate increase in the succeeding years to below 1% per year. If the payment limit is weakened, the maximum interest rate increases permitted in these succeeding years will be greater.

All in all, from the borrower's perspective accepting a weaker payment limit in return for a direct interest rate increase limit would be a poor trade-off. The trade-off would allow a higher cumulative interest rate increase over a 4 to 6 year period and greater short run payment volatility. The only benefit would be the possibility of slightly lower negative amortization in several years over the life of the mortgage. It is not even possible to say that this lower negative amortization is likely to result in lower payments in future years, because the weaker payment limit will allow higher interest rates in future years, thereby increasing loan balances and payments.

Thus, strict payment and loan balance limits will provide borrowers with adequate protection against payment, loan balance, and interest rate increases. The underlying goal of imposing an additional direct limit on interest rate increases - to prevent excessive negative amortization in a single year - is already met by the loan balance limit. Imposing a direct interest rate limit is likely to result in a weaker payment limit which in turn would cause a net loss in overall borrower protection.

ADJUSTABLE RATE MORTGAGE SIMULATIONS

PUBLIC INTEREST RESEARCH GROUP

MAY 1981

ARM Simulations with the Proposed Payment and Loan Balance Limits

Three ARM simulations are provided using the proposed limits on monthly payment and loan amount increases per year. In each simulation the original loan amount is $50,000 and original interest rate is 9.15%, the average rate on conventional mortgages made in January 1978. Interest rate index values for 1979, 1980, and 1981 were determined using actual movements in the conventional mortgage rate (Simulations II and III) and the 6th month Treasury bill rate (Simulation I).

In all simulations the monthly payment is adjusted each January and can never rise at a rate greater than 2/3 the wage increase rate for the preceding year. The loan balance can never rise at a rate greater than 1/5 the CPI increase rate for the preceding year. To simplify the calculations, the home appreciation rate is not considered. It is unlikely that the appreciation rate would differ substantially from the inflation rate over an extended period.

The interest rate on the ARM is always the same as the index interest rate, unless a separate rate is listed in the ARM Effective Interest Rate column. A separate rate is shown whenever the payment and loan balance limits have indirectly constrained the ARM rate so that it cannot rise as fast as the index rate.

The extent to which the proposed payment and loan balance limits constrain sharp cyclical interest rate increases varies dramatically with the type of index used. The restraint is much greater with a short term rate index, such as the 6 month Treasury bill rate, than with a long term rate index, such as the fixed rate mortgage or long term bond rate. Short term rates are far more volatile than long term rates and a precipitous decline in a short term rate index can drive the monthly payment to a very low level. When the index begins to rise, the payment and loan balance limits will soon become restraining. If the payment has fallen greatly during a cyclical trough, the limits may hold the ARM rate below its previous high for several years. By way of contrast, with a more stable, long term rate index, monthly payments will fall less dramatically in cyclical troughs and the ARM rate can rise higher on the upswing before it is constrained by the limits.

If ARMs have the limits on payment and loan balance increases necessary to protect borrowers, lenders will find that a long term index provides better ARM earnings than a short term index. During a cyclical trough the ARM rate will be lower with a short term index than with a long term index. During a cyclical peak, the ARM rate with a short term index could well be constrained by the limits to be lower than the rate with a long term index, even though the short term index would be much higher than the long term index.

Of course, this problem could be remedied from the lender's perspective by a rule that prohibited monthly payments from declining. If monthly payments were held constant in the face of sustained rate declines, borrowers would pay off their mortgages at faster rates than originally scheduled. However, freezing the monthly payment at its highest level would make the ARM far less desirable to borrowers who obtain an ARM during a high rate period and hope that both the rate and the monthly payment will decline in the future. Basing the ARM index on a long term rate is the best approach. A long term rate index will moderate cyclical rate fluctuations and greatly reduce the likelihood that payment and loan balance limits will constrain lenders' yields.

ARM SIMULATION I

ndex: 6th Month Treasury Bill Rate
conomic Scenario: Cyclical Inflation

ar	Index Interest Rate	ARM Effective Interest Rate	CPI (Growth Rate)	Wages (Growth Rate)	Monthly Payment	Loan Balance (End of Yr)
1978	9.15%	-	9.0%	8.9%	$408	$49,669
1979	12.11	-	13.3	7.4	432	50,559
1980	14.59	13.3	12.4	8.2	453	51,895
1981	17.39	13.4	10	8	478	53,182
1982	17	13.2	8	8	503	54,245
1983	12	-	7	8	530	54,405
1984	8	-	11	8	425	53,624
1985	15	12.1	15	9	448	54,803
1986	20	13.2	15	11	475	56,448
1987	22	13.7	10	13	510	58,141
1988	10	-	7	10	554	57,266
1989	6	-	8	8	422	55,60[illegible]
1990	10	-	8	8	444	55,845
1991	11	-	12	8	467	56,407
1992	16	12.7	13	9	492	57,761
1993	18	13.3	18	10	522	59,263
1994	25	14.6	18	13	557	61,396
1995	28	15.2	15	15	605	63,607
1996	18	15.4	10	13	666	65,513
1997	8	-	10	11	724	61,942
1998	10	-	12	10	776	58,677
1999	16	-	10	10	828	58,011
2000	12	-	10	10	884	54,237
2001	10	-	8	10	900	48,603
2002	6	-	12	10	805	41,664
2003	16	-	14	10	859	37,737
2004	20	-	16	12	917	33,945
2005	22	-	16	14	990	29,054
2006	24	-	15	14	1083	22,329
2007	20	-	-	-	1183	11,654

ARM SIMULATION II

Index: Long Term Interest Rate (10-20 year Treasury Bond or
Fixed Rate Mortgage)
Economic Scenario: Cyclical Inflation

Year (Jan)	Index Interest Rate	ARM Effective Interest Rate	CPI (Growth Rate	Wages (Growth Rate)	Monthly Payment	Loan Balance (end of Yr)
1978	9.15%	-	9.0%	8.9%	$408	$49,669
1979	10.33	-	13.3	7.4	432	49,616
1980	12.10	-	12.4	8.2	453	50,216
1981	13.67	-	10	8	478	51,420
1982	13	-	8	8	503	52,107
1983	11	-	7	8	511	51,690
1984	10	-	11	8	474	51,646
1985	12	-	15	9	499	51,863
1986	15	-	15	11	529	53,394
1987	17	15.6	10	13	568	54 996
1988	14	-	7	10	617	55,307
1989	12	-	8	8	617	54,497
1990	12	-	8	8	617	53,585
1991	12	-	12	8	617	52,558
1992	14	-	13	9	650	52,092
1993	15	-	18	10	633	51,552
1994	18	-	18	13	740	51,993
1995	19	-	15	15	804	52,246
1996	18	-	10	13	884	50,935
1997	15	-	10	11	790	48,964
1998	14	-	13	10	760	46,544
1999	15	-	10	10	788	43,896
2000	14	-	10	10	763	40,690
2001	13	-	8	10	740	36,875
2002	12	-	12	10	721	32,409
2003	14	-	14	10	754	27,596
2004	16	-	16	12	782	22,245
2005	18	-	16	14	804	16,109
2006	19	-	15	14	812	8,811
2007	18	-			908	0

BEST DOCUMENT AVAILABLE

ARM SIMULATION III

Index: Long Term Interest Rate (10-20 year Treasury Bond or
Fixed Rate Mortgage)
Economic Scenario: Rising Inflation for 15 Years

Year (Jan)	Index Interest Rate	ARM Effective Interest Rate	CPI (Growth Rate)	Wages (Growth Rate)	Monthly Payment	Loan Balance (End of Yr)
1978	9.15%	-	9.0%	8.9%	$408	$49,669
1979	10.33	-	13.3	7.4	432	49,616
1980	12.10	-	12.4	8.2	453	50,216
1981	13.67	-	11	9	478	51,420
1982	14	13.9	12	9	507	52,552
1983	15	14.5	14	10	537	53,813
1984	17	15.4	16	12	573	55,320
1985	19	16.4	18	14	619	57,090
1986	21	17.5	20	16	676	59,145
1987	23	18.9	22	18	749	61,511
1988	25	20.4	24	20	838	64,217
1989	27	22.1	26	24	950	67,300
1990	29	24.3	28	26	1102	70,799
1991	31	26.9	30	28	1293	74,764
1992	33	29.8	30	28	1534	79,250
1993	33	32.7	25	25	1821	84,005
1994	28	-	20	20	2002	83,437
1995	23	-	20	20	1686	82,273
1996	23	-	20	20	1686	80,810
1997	23	-	20	20	1686	78,973
1998	23	-	20	20	1686	76,666
1999	23	-	20	20	1686	73,769
2000	23	-	20	20	1686	70,131
2001	23	-	20	20	1686	65,562
2002	23	-	20	20	1686	59,824
2003	23	-	20	20	1636	52,617
2004	23	-	20	20	1686	43,567
2005	23	-	20	20	1686	32,201
2006	23	-	20	20	1686	17,926
2007	23	-			1686	0

BEST DOCUMENT AVAILABLE

Mr. SCHUMER. That is really all I have to say, other than, please do not—let us not sink the ship if we have real troubles in the Senate, because I know that our chairman has basically the same interest that I and I believe you have at heart.

Chairman GONZALEZ. Mr. Nader, do not expose me to partiality. We have this other side, too, that we must give fair and equal chance. We did have referral made by one of the members. Mr. Wortley indicated he had a question.

Mr. WORTLEY. I have a couple of questions.

Mr. NADER. Mr. Chairman, just a point of privilege. I really have to meet this Senator. Otherwise he will draw and quarter us. But Jonathan Brown, who is the coauthor of this testimony. would be glad to stay and answer your questions.

Mr. WORTLEY. I will take on Mr. Brown.

Chairman GONZALEZ. Thank you.

Mr. WORTLEY. I am not so sure I agree with the logic of your conclusion that mutual savings banks are better able to weather the long-term interest rate risk than stock institutions. It may sound like a good theory, but if we take a look at practical facts and what is going on today, with forced mergers, the failing institutions, have been essentially in the area of the large mutuals, more so than with stock institutions. The hit list has been the large mutuals before it has been the savings and loans.

Do you want to comment on that?

Mr. BROWN. Yes. That is a very interesting question. We will within the next week submit an analysis of that development, looking at the extent to which mutuals versus stocks have been more troubled. It is difficult to make generalizations. Obviously, you look at the New York situation, where you have the large mutual savings banks that are probably the most troubled of all the thrift institutions.

But I think it is important to remember the fact that these troubles are endemic to particular markets. These are structural, regulatory, usury rate factors that have applied to New York State, that are different from other markets. And it happens that savings banks in New York cannot be organized on a stock basis. So all of the institutions in New York have been mutual institutions. Therefore, that makes mutuals look bad.

But I am afraid it was more the New York environment than the fact that they were mutuals. If they had been stock institutions in New York, I think they would have been equally troubled.

One further point, and that is that in other States, in New England, where you have savings banks that have had a different regulatory environment, not as restrictive usury ceilings in the past, where they have more low-cost deposits, the mutuals are still doing fairly well. In Massachusetts and in other States, some of them have very strong capital ratios. Some of them have even, I believe, still some profitability.

So that it is an important question and we will address it.

Mr. WORTLEY. In the past, you have expressed your opposition to variable rate mortgages. But the industry would not be in the doldrums today, it wouldn't have the problems it is confronted with if we had variable rate mortgages in effect for the past several years, according to Mr. Pratt, who testified here not too long ago. He calculated that if the S. & L.'s since 1975 had been making ARM's with a 1-percent-per-year limit on interest rate increases, that their 1980 mortgage portfolio yield would be 1.3 percent higher than it is today.

Some of your advocacy has created the problem in the marketplace today. We wouldn't have to be talking about a bailout of thrifts if we had had variable rate mortgages.

Mr. **Brown**. I think there is an element of truth in that. But I think also that there are other people that share the blame, too. There are a lot of regulators, even industry officials who felt 10 years ago that fixed rate mortgage lending made sense. None of us anticipated the volatility in interest rates, the fairly Draconian monetary policy that we are experiencing right now. We recognize now that there is a need for flexibility. That is why we are proposing in essence that 50 percent of the assets of savings and loans be invested in very flexible instruments with essentially no contraints on rate increases and no constraint on the maturity.

As for the other 50 percent, we are proposing that they be invested in adjustable rate mortgages, which, similar to the type that Mr. Pratt was analyzing there, would have some flexibility, where there would be a sharing of interest rate risk. We feel that this combination would still allow S. & L.'s to be competitive. If they are simply investing in fixed rate mortgages only, then obviously I don't think they could survive.

Mr. **Wortley**. Just two very short questions. You can give me a yes or no. Do you favor the elimination of usury rates?

Mr. **Brown**. On mortgage loans?

Mr. **Wortley**. Yes.

Mr. **Brown**. Yes. That has been done by Federal statute, and although generally we don't favor preemption of State laws unless a strong burden has been met, I think that in this case the mortgage usury ceilings caused more trouble than they did good, and the elimination of them was legitimate.

Mr. **Wortley**. If you had your choice of enacting the capital assistance program for thrifts or the regulators bill which we passed in the House, what would be your choice?

Mr. **Brown**. That is a difficult question to answer. I would have to think about that. I am not sure. My first choice would be the capital assistance bill with the public benefits which we proposed. In the absence of the public benefits, I might choose the regulators bill, which essentially would be a continuation of the current supervisory merger process. We would be indifferent to some extent, but very concerned that the capital assistance bill, if it passed, would really be providing public benefits to private stockholders in the long run.

So, I guess, without the public benefits, we would probably be leaning toward the regulators approach.

Mr. **Wortley**. Thank you very much.

Thank you, Mr. Chairman.

Chairman **Gonzalez**. Thank you, sir.

I want to thank all of the very patient panelists that have been so nice.

I would next recognize Ms. Cincotta.

STATEMENT OF GALE CINCOTTA, CHAIRPERSON, NATIONAL PEOPLE'S ACTION

Ms. CINCOTTA. Thank you, Mr. Chairman and members of the subcommittee, for this opportunity.

We feel that the intent of the home mortgage capital stability fund is commendable, and I agree with Congressman St Germain's comments when he introduced H.R. 5568 that it is "imperative that the Congress act quickly and in a fashion that will move funds immediately into the mortgage lending industry."

Unfortunately, we feel that this bill does not meet that imperative. I do not see a sufficient enough increase in mortgage lending resulting from the bill to justify the $7.5 billion price tag placed on this piece of legislation. It does not matter whether the capital assistance is in the form of cash infusion or capital guarantees. This bill seems designed to bail out the thrift industry and not to benefit those Americans right now searching for an affordable loan.

Our country is in the midst of a financial revolution, and nowhere has there been a priority placed on housing. All the tinkering that has been done to the savings and loans since Robert McKinney was Chairman of the Federal Home Loan Bank Board has been for the worse. Neighborhood people said it loud and clear way back in 1977 that to deregulate the lending industry without providing for a continuous supply of affordable mortgage money would be economic ruin.

Now the thrift industry is coming out of those ruins to seek Federal assistance. The DIDC, the Depository Institutions Deregulation Committee, is meeting again on Monday. What is the top agenda item? Another short-term deposit instrument to let banks compete with money market funds. The ABA is lobbying fiercely for it. The thrifts want a differential in their favor, but may be willing to deal for the banking industry's support for their proposal. All the lenders are jockeying for position, but no one seems to care about the folks who will have no hopes of having an affordable mortgage.

If the banks and thrifts are going to raise the money market funds, a lot of us are going to be eating dust for a long time. Every 1 percent increase in interest rates puts 860,000 families out of the reach of homeownership. That is one of the findings we discovered as part of the Illinois Governor's Task Force on Interest Rates and Home Ownership. Our final report is going to be released soon, and I can get a copy to the subcommittee.

Let me tell you all some other effects of our current economic crisis that the task force discovered in Illinois. When interest rates are over 17 percent, those rates disqualify 90 percent of first-time home buyers for a loan. The current recession has cost the State of Illinois $90 billion over the last 3 years in lost sales tax, income tax, and real estate revenue, and additional unemployment compensation costs.

In single-family homes $1 billion worth of investments would create 19,100 on-site construction jobs, 14,000 indirect jobs, and 103,000 sale-induced jobs. The Governor's task force showed that high interest rates have cost the residents of Illinois jobs and money.

The dollar figures nationally are even more staggering. According to the National Association of Realtors, 3 million home sales could not take place over the last 3 years because of high interest rates. They estimate that to equal $230 billion worth of business, and that is not even counting revenues lost from lack of furniture, home appliances, home improvement sales, et cetera.

The number of jobs at stake for the housing industry is also staggering nationally. I assume you have the figures I have in this testimony.

The other thing is, there are all sorts of figures on creative financing as the primary source of mortgage money. The National Association of Realtors found that as of October 1981, creative financing was used in 60 percent of all transactions. They also found that in 65 percent of people-to-people transactions, the seller is the source of lending, while 43 percent of all single-family homes sold involved assumptions of an existing mortgage.

We have found that 75 percent of all transactions on the southwest side of Chicago and 90 percent on the northwest side use creative financing. This use of creative financing is already coming back to haunt us. According to data from the Department of Housing and Urban Development, delinquent mortgages are cropping up. In Illinois, delinquent mortgages have risen to 9.14 percent of the total number of mortgages in the State; 11.6 of all FHA mortgages are in default, and 4.8 of conventional mortgages, the highest in the country.

Nationally, 1 out of every 20 mortgages is delinquent. This is a vicious circle that is killing the backbone of this country. Interest rates are putting people out of work, so they become delinquent in their mortgages. Creative financing becomes the only lending game in town, because of high rates. Balloon payments come due or rates are adjusted up. People don't have the cash, and the economy worsens.

In light of these figures, the mortgage requirements proposed in H.R. 5568 are inadequate. As drafted, the bill requires institutions receiving capital assistance to use 50 percent of their net new deposits to make mortgage loans for the first-time buyers with an interest rate not more than 1 percent greater than their average cost of funds. The National Savings & Loan League opposes even this attempt to extract a quid pro quo from the industry.

To increase mortgage lending, Federal legislation should require that all savings and loans and savings banks serve the mortgage market, not just those institutions receiving financial assistance. The legislation should be designed not to earmark a percentage of their new deposits which have been minimal, almost nonexistent, but to earmark a percentage of their total assets for affordable mortgages.

This hearing today, I feel, was called together to consider how best to save thrifts. I feel that we should save the thrifts only if we are saving them for housing, and the only way to do that is to require all thrifts to invest at least 50 percent of their total assets in direct long-term mortgages at fixed rates or renegotiated rates with constraints.

This requirement should be for direct mortgages, not just buying up the paper of existing mortgages. We think that the proposal of the U.S. League of Savings Associations and the National Association of Mutual Savings Banks is more conducive to generating affordable housing dollars than H.R. 5568. The concept of the mortgage buy-down plan that they have proposed is similar to a concept of an affordable line of credit that we have been pursuing with the Federal Reserve Board, with lenders offering mortgage rates at 1 percent below market and the Treasury providing a 3-percent supplement. The buyers would actually pay 4 percentage points less than the market rates.

I believe that a mortgage buy-down plan is essential to a housing recovery, but there must be a targeting of such a plan to those most in need of affordable loans. The industry's plan should be limited to the one home you live in and to housing within a certain price range, using the HUD 203 guidelines. The program should not be limited to first-time home buyers or solely for new construction. Our existing housing stock requires affordable loans as well as new housing starts.

Mortgage buy-downs should not automatically revert back to market rates after 3 years. If there must be adjustable rates, they should be limited to increases of only a half a percentage point a year, with a maximum increase of 2½ percent over a 25-year term.

There is a need for a mortgage mandate for the private sector and public sectors. There must be a renewed supply of mortgage loans that do not expose homeowners to excessive interest rates or refinancing uncertainty. The charter obligation of financial institutions to serve the credit needs of their entire local community, including low and moderate-income areas, older urban neighborhoods, and minorities, is going unmet. This obligation was reaffirmed by Congress when it passed the CRA of 1977, yet Congress and the financial regulators find it convenient to overlook this unmet obligation as financial institutions scramble for more powers. Thrifts want to be like banks, and banks want to be like money market funds and stockbrokers, and the credit needs of the majority of Americans are not dealt with.

The credit crisis and the plight of the thrifts in this country cannot be discussed in isolation here. If the thrifts are going to become more like banks, then there will have to be a mortgage mandate for the banks. The banks will have to accept additional responsibility also for mortgage lending. The major banks in this country are profiteering from this credit crisis.

First National Bank of Boston had its highest earnings in its history. Fourth quarter earnings in 1981 for Chase Manhattan were up 99.2 percent. For Continental Illinois Bank they were up 35.7 percent, and for Manufacturers Hanover they were up 19.2 percent. The chief economist for Manny Hanny was quoted last Sunday in the New York Times as calculating that the real rate of interest is now 8.08 percent.

In the past, the spread between the prime rate and inflation, the real rate of interest averaged about 2 percent. No wonder the thrifts want to be more like banks. There is fast money being made out there.

Walter Wriston, chairman of Citibank and head of the Business Roundtable. admits that the Nation now has the highest real rate of interest in the last 25 years, but if we would stabilize that real rate of interest at the historical 2 percent, the banks could be providing interest rates today of 10 percent on mortgages.

Senator Roth has already reacted to profits of larger banks rising as high as 200 percent by suggesting a windfall profits tax on bank interest. Representative Wright here in the House has proposed a tax of 80 percent on all interest income received above 15 percent on any loan.

We do not advocate increasing taxes on banks as a way out of our economic crisis. Rather, I am stressing that banks are in a position to provide an affordable line of credit, not only for housing but for small business and the family farm that are also the victims of high interest rates.

Through the network of National People's Action, we have been attempting to cooperatively develop this concept with some major commercial banks and the Federal Reserve Board. Most banks have been refusing to even sit down at the table and explore the concept. Unless things change dramatically, when we meet again with Paul Volcker next Monday, the Federal Reserve will also continue to ignore the credit needs of the small borrower.

That is why we have supported House Joint Resolution 365 and Senate Joint Resolution 120 that were introduced last year and that recognized the need to assure a flow of credit at affordable prices.

From our experiences so far, the banks and the Federal Reserve are not going to address this crisis, credit crisis voluntarily. I urge Congress to hold hearings immediately with the banks on why they cannot provide affordable mortgages for Americans right now. I would also urge Congress to hold hearings on the whole issue of deregulation, deregulating depository institutions. Deregulation has not been a cure, but another virus preventing a healthy economy.

DIDC has done nothing to help housing. It will only raise costs further and hurt the consumer more in terms of their credit needs. Also, if all the new financial creatures, Sears, Merrill Lynch, Prudential, American Express, want to soak up our savings, they should be held accountable for their investments. Congress also needs to reconsider the whole regulation question, including money market funds.

In conclusion, I ask you, "Who will finance housing at affordable cost?" Until Congress has answered that question, I predict that we will continue to meet again and again on bailouts for the industry, short-term answers, and soon, how to deal with depression-time foreclosure rates and the possible need for massive public housing.

Thank you.

[The prepared statement of Ms. Cincotta follows:]

STATEMENT OF GALE CINCOTTA, EXECUTIVE DIRECTOR, NATIONAL TRAINING & INFORMATION CENTER AND CHAIRPERSON, NATIONAL PEOPLE'S ACTION

The intent of the Home Mortgage Capital Stability Fund is commendable. I agree with Congressman St Germain's comments when he introduced H.R. 5568 that "it is imperative that the Congress act quickly and in a fashion that will move funds immediately into the mortgage lending industry."

Unfortunately, this bill does not meet that imperative. I do not see a sufficient enough increase in mortgage lending resulting from this bill to justify the $7.5 billion price tag placed on this piece of legislation. It does not matter whether the capital assistance is in the form of cash infusion or capital guarantees. This bill is designed to bail out the thrift industry, not to benefit those Americans searching for an affordable mortgage.

This country is in the midst of a financial revolution and nowhere has a priority been placed on housing. All the tinkering that has been done to the savings and loans since Robert McKinney was Chairman of the Federal Home Loan Bank Board has been for the worse. Neighborhood people said it loud and clear back then in 1977 that to deregulate the lending industry without providing for a continuous supply of affordable mortgage money would be economic ruin. Now the thrift industry is coming out of those ruins to seek federal assistance.

The Depository Institutions Deregulation Committee (DIDC) is scheduled to meet again on Monday, March 22 as you well know. What is the top agenda item? --- another new short-term deposit instrument to let banks compete with money market funds. The American Bankers Association is lobbying fiercely for it. The thrifts want a differential in their favor but may be willing to deal for the banking industry's support for their bail-out proposal. All the lenders are jockeying for position but no one cares about the folks left behind in the dust, with no hope of ever affording a home.

If the banks and thrifts are going to race the money market funds, a lot of us are going to be eating dust for a long time. Every one percent increase in interest rates puts 860,000 families out of reach of home ownership. That is one of the findings I discovered as part of Illinois Governor Jim Thompson's Task Force on Interest Rates and Homeownership. [Our final report will be released soon.]

Let me tell you all some other effects of our current economic crisis that the Task Force discovered in Illinois:

* When interest rates are over 17%, those rates disqualify 90% of first-time homebuyers for a loan.
* The current recession has cost the State of Illinois $90 billion over the last three years in lost sales tax, income tax and real estate revenue and additional unemployment compensation costs.
* $1 billion worth of investments in single family homes would create 19,100 on-site construction jobs; 14,000 indirect jobs; and 103,000 induced jobs.

The Governor's Task Force in Illinois discovered that high interest rates have cost the residents of Illinois jobs and money. The dollar figures nationally are even more staggering. According to the National Association of Realtors, three million home sales could not takeplace over the last three years because of high interest rates. They estimate that to equal $230 billion worth of business, and that is not even counting revenues lost from lack of furniture, home appliances, home improvement sales, etc.

The number of jobs at stake for the housing industry is also staggering nationally:

- The National Association of Realtors estimates that 2.8 million jobs were lost in 1981 as a result of high interest rates on the real estate industry.
- The National Association of Home Builders estimates that as of February, 1982, the housing construction-related field had 928,000 workers out of work. That means that one out of every ten unemployed people is a housing construction-related worker.

There are all sorts of figures on creative financing as the primary source of mortgage money:

- The National Association of Realtors found that as of October, 1981, creative financing was used in 60% of all transactions.
- They also found that in 65% of people-to-people transactions, the seller is the source of lending while 43% of all single family homes sold involved assumptions of an existing mortgage.
- We have found that 75% of all transactions on the Southwest side of Chicago and 90% on the Northwest side use creative financing.

This use of creative financing is already coming back to haunt us. According to data from the Department of Housing and Urban Development (HUD), delinquent mortgages are cropping up:

- In Illinois, delinquent mortgages have risen to 9.14% of the total number of mortgages in the state.

* Nationally, 5.48% of all mortgages are delinquent in this country. One out of every 20 mortgages is deliquent.

This is a vicious circle that is killing the backbone of the country. Interest rates are putting people out of work, so they become delinquent in their mortgage. Creative financing becomes the only lending game in town because of high rates. Balloon payments come due or rates are adjusted up. People don't have the cash. The economy worsens some more.

In light of these figures, the mortgage requirement proposed in H.R. 5568 is inadequate. As drafted, the bill requires institutions receiving capital assistance to use 50% of their net new deposits to make mortgage loans for first time buyers with an interest rate not more than 1% greater than their average cost of funds. Of course, the National Savings & Loan League opposes even this meager attempt to extract a quid pro qou from the industry.

If Congress is serious about increasing mortgage lending, federal legislation should require all savings and loans and savings banks to serve the mortgage market, not just those institutions receiving financial assistance. The legislation should be designed not to earmark a percentage of their net new deposits, which have been minimal if not almost non-existent, but to earmark a percentage of their total assest in affordable mortgages.

This hearing was called today to consider how to best save thrifts. What I am saying is that we should save the thrifts only if we are saving them for housing. The only way to do that is to require all thrifts to invest at least 50% of their total assets in direct long-term mortgages at fixed rates or renegotiated rates with constraints on increases. I am suggesting that this requirement for direct mortgages, not just buying up the paper of existing mortgages, is the fastest way to increase mortgage lending.

I find the proposal of the U.S. League of Savings Associations and the National Association of Mutual Savings Banks to be more conducive to generating affordable housing dollars than H.R. 5568. The concept of the "mortgage buy-down" plan that they have proposed is similar to a concept of an "Affordable Line of Credit" that we have been pursuing with the Federal Reserve Board. With lenders offering mortgage rates at one percent below market and the Treasury providing a three percent supplement, the buyers would actually pay four percentage points less than market rates.

I believe that a "mortgage buy-down" plan is essential to a housing recovery. But there must be a targeting of such a plan to those most in need of affordable loans. The industry's plan should be limited to the one home you live in and to housing under certain prices. The program should not be limited to first time homebuyers or solely for new construction. Our existing housing stock requires affordable loans as well as new housing starts. Mortgage buy-downs should not revert back to mortgage rates after three years. If there must be adjustable rates, they should be limited to increases of only a half percentage point a year with a maximum increase of 2½% over a twenty-five year term.

There is a need for a new mortgage mandate by the private and public sectors. There must be a renewed supply of mortgage loans that do not expose home owners to excessive interest rates or refinancing uncertainity. The charter obligation of financial institutions to serve the credit needs of their entire local community, including low and moderate income areas, older urban neighborhoods, and minorities is going unmet.

This obligation was reaffirmed by Congress when it passed the Community Reinvestment Act of 1977. Yet, Congress and the financial regulators find it convenient to overlook this unmet obligation as financial institutions scramble for more powers. Thrifts want to be like banks and banks want to be like money market funds and stock brokers. And the credit needs of the majority of Americans are shrugged off.

The credit crisis and the plight of the thrifts in this country cannot be discussed in isolation here. If the thrifts are going to become banks, then there will have to be a mortgage mandate for banks. The banks will have to accept responsibility also for mortgage lending.

The major banks in this country are profiteering from this credit crisis. First National Bank of Boston had its highest earnings in its history. Fourth quarter earnings in 1981 for Chase Manhattan were up 99.2%; for Continental Illinois, they were up 35.7%; and for Manufacturers Hanover, they were up 19.2%.

The chief economist for Manny Hanny was quoted last Sunday in The New York Times as calculating that the real rate of interest is now 8.08%. In the past, the spread between the prime rate and inflation (the real rate of interest) averaged around 2%. No wonder the thrifts want to be more like banks -- there's fast money being made out there today.

Even Walter Wriston, chairman of Citibank and head of the Business Roundtable, admits that the nation now has the highest real rate of interest in the last twenty-five years. But if we would stabilize that real rate of interest at the historical 2%, the banks could be providing interest rates today of 10%.

Senator Roth has already reacted to profits of larger banks rising as high as 200% by suggesting a windfall profits tax on bank interest. Representative Wright here in the House has proposed a tax of 80% on all interest income received above 15% on any loan. I do not advocate increasing taxes on banks as a way out of our economic crisis. Rather, I am stressing that banks are in a position to provide an "Affordable Line of Credit" not only for housing but for small businesses and the family farm that are also the victims of high interest rates.

Through the network of National People's Action, we have been attempting to cooperatively develop this concept with some major commercial banks and the Federal Reserve Board. But the banks have been refusing to even sit down at the table and explore the concept. Unless things change dramatically when we meet with Paul Volcker next Monday, the Federal Reserve will continue to ignore the credit needs of the small borrower.

That is why we have supported House Joint Resolution 365 and Senate Joint Resolution 120 that were introduced last year and recognize the need to assure an adequate flow of credit to small borrowers at affordable prices. From our experience though, the banks and the Federal Reserve are not going to address this credit crisis voluntarily. I urge Congress to hold hearings immediately with the banks on why they cannot provide affordable credit for Americans.

I urge Congress to hold hearings on the whole issue of deregulation of depository institutions. Deregulation has not been a cure but another virus preventing a healthy economy. DIDC has done nothing to help housing; it will only raise costs further and hurt the consumer more in terms of our credit needs.

Also, if all the new financial creatures -- Sears, Merrill Lynch, Prudential, American Express -- want to soak up our savings, they should be held accountable for their investments. Congress needs to reconsider the whole regulation question including money market funds.

In conclusion, I ask you "Who will finance housing at affordable costs?" Until Congress has answered that question, I predict that we will continue to meet again and again on bailouts for the industry, short-term answers, and how to deal with depression-time foreclosure rates and the need for massive public housing.

I ask you "How long will we have to meet before we have an answer?" I'm ready and waiting.

Chairman GONZALEZ. Thank you, Ms. Cincotta, for an excellent statement.

We would next recognize Mr. Sisson of the Communications Workers of America.

STATEMENT OF HALL SISSON, LEGISLATIVE REPRESENTATIVE, COMMUNICATIONS WORKERS OF AMERICA

Mr. SISSON. Thank you, Mr. Chairman.

My name is Hall Sisson. I am a legislative representative for the Communications Workers of America, a labor union which represents some 645,000 working men and women in the telecommunications industry and in the public service sector.

I am here today to add my support and that of my union to the joint statement concerning H.R. 5568, prepared by those of us sitting on this panel. Mr. Chairman, I would like to put the rest of my prepared statement into the record and just make some observations, if that is all right with you.

Chairman GONZALEZ. Without objection, so ordered.

[The prepared statement of Mr. Sisson follows:]

Testimony of
Hall H. Sisson, Legislative Representative
Communications Workers of America
before the
Subcommittee on Housing and Community Development
of the House Banking, Finance and Urban Affairs Committee
March 18, 1982

Mr. Chairman, Members of the Subcommittee:

My name is Hall Sisson, and I am a legislative representative for the Communications Workers of America (CWA), a labor union which represents some 645,000 working men and women in the telecommunications industry and in the public service sector.

I am here today to add my support and that of my Union to the joint statement concerning H.R. 5568 prepared by those of us sitting on this panel.

I hope that all of you and your staffs take the time to thoroughly read it. I feel it sets forth a rational way to assist troubled thrift institutions while at the same time maintaining their commitment to providing funds for home mortgages.

To again recite the whole litany of the disaster which has overtaken the home building industry would be a waste of your time. So to would be a reiteration of the dispair felt by the home-buying industry. Those young working men and women - many of whom are members of my Union - who have been frozen out of the opportunity to own a home by a lack of available housing and high mortgage interest rates.

No one denies that savings and loan associations and mutual savings banks are facing rocky times. The work being done by Chairman St Germain to aid the industry should be applauded. And the federal government does have a commitment to stand behind the savings of depositors both large and small.

But most importantly, during all of these hearings and all of this talk on legislation to bail the thrift industry out of its troubles, the continued commitment of this industry to providing the funds for the housing needs of this country cannot be left at the wayside like some abandoned orphan. What is needed instead is the new mortgage mandate that is being advocated today by this panel.

Our approach to H.R. 5568 is fairly simple and straightforward. Since public monies are to be used to assist savings and loans and savings banks, then the public interest must be served by all of these institutions, both the strong and the weak.

The first commitment to the new mortgage mandate would require that savings and loans and savings banks invest at least 50% of their total assets in either long-term adjustable rate mortgages or in fixed-rate mortgages. These adjustable rate mortgages would have adequate consumer safeguards that would handle the twin problems of negative amortization and wildly fluctuating monthly payments.

Secondly, would be the public disclosure of how savings and loans and savings banks are meeting their duty to serve the mortgage credit needs of their communities. By making available to public scrutiny the CRA (Community Reinvestment Act) ratings and performance evaluations of these lenders, you would be opening up the mortgage lending process to meaningful review and evaluation.

And finally, we would discourage the conversion of mutually owned savings and loans and savings banks into stock institutions.

All of these proposals are adequately explained in our joint statement.

Mr. Chairman, you and the members of your Subcommittee are faced with a unique opportunity to put your mark on the future of mortgage lending in this country. Not only can you act to shore-up the mainstay of the home building and home buying industry, but you can also make that industry more open and more responsive to the general needs of the American public as a whole.

I thank you for the time you have granted me to appear before you, and I would welcome any questions you may have.

Mr. SISSON. First of all, in deference to my good friend, Ralph Nader, and John Brown, I can say the Communications Workers of America is not too happy about sticking envelopes in telephone bills in order to raise money to provide public service advocacy in those areas. We seem to think that we know a little bit more about the telecommunications industry, and we will work our way through that bill over in Mr. Wirth's subcommittee just fine, thank you.

Mr. Chairman, you mentioned this being a new mandate. I look at it just as a plain mandate, as one who has sat through innumerable hours of hearings over in the other body. You would get the impression from the banks and the savings and loans and the mutual savings banks and everybody else that they just don't want to make mortgages any more. I mean, just flat out, they want to get out of the mortgage business.

We see certain things, like eliminating due-on-sale clauses and State usury rates, and the whole litany of the package to dismantle consumer protection legislation that we have spent the last 10 years putting on the books, primarily in this committee, and with the help of yourself and Chairman St Germain and Wright Patman and Henry Reuss and others, and you know, it was a surprise to us when we sent up a letter to the Senate Banking Committee listing all of the consumer problems that we saw with that bill over there.

We made the front page of the American Banker. Those people were flabbergasted. They didn't even know consumers existed. They were so busy dismantling all of the consumer protections that they forgot about us.

Another observation is, I think you mentioned that this was an emergency bill. Well, we saw an emergency bill go over there a few months back that Mr. St Germain put forth as an emergency bill, and now here we have another emergency bill We are just wondering what the other body is going to be doing about all of this. I think Chairman St Germain said he was a little bit worried about the form and substance of it when it came back over to a conference committee and certainly we are worried about that also. That is why we have to come in here before your group and get an opportunity to get our licks in and get publicity, because we certainly aren't getting a hearing before the other body.

You will notice in our testimony that we ask that there be a 50-percent limitation across the board for all savings and loans. I feel this is only fair. The representatives of the industry came in here, and I am sure—I didn't get to hear them this morning as I was busy with something else—and I didn't get to hear their testimony, but I understand they went on for some hours, and all I can ask is, did any troubled savings and loans come before your group? Did anybody stand here at this table and say, I am in trouble, I need your help? Or did the industry speak for them?

Well, if the industry is going to speak for the entire savings and loan industry, and if the entire savings and loan industry wants this help, then they should buy this 50-percent across the board mortgage, qualified mortgage package that we are talking about.

I have to admit—I know Chairman St Germain knows this—that many years ago I fought long and hard against variable interest rate mortgages, and was successful in blocking them for many years, and now I have to admit that it looks like we are going to have to go to variables, and in fact, if that is going to help the savings and loan industry, which I think all of us at this panel want to do, we don't want to see the savings and loan industry or the savings banks go under. We know that somebody has to make mortgages out there, even though they want to make automobile loans and don't want to make mortgages.

You know, we know that there has to be somebody who makes mortgages, but with the safeguards we have proposed, we think that variable rate mortages—and the American public can live with variable rate mortgages. In fact, I think that maybe a good thing to do is to study the California experience, to see if that is working quite well.

In just closing my brief remarks, for Chairman Gonzalez, who knows my good friend, Henry Schechter will be in here next week, and so I will not submit anything on housing. I will let Henry do that job on behalf of the AFL-CIO and our union. Thank you very much.

Chairman GONZALEZ. Thank you, Mr. Sisson.

Both the CWA and the AFL-CIO have always contributed quite a bit to our hearings. As to the other body, the House of Lords, both temporal and spiritual, we can't answer for them.

[General laughter.]

Chairman GONZALEZ. We have had that dilemma for a few years, but I think that it is getting indemic, and this is the reason that I think Chairman St Germain was so ably describing the limitations within which, no matter what we desire individually, we have to forge legislation in order to survive this process.

Mr. Sloane?

STATEMENT OF MARTIN E. SLOANE, EXECUTIVE DIRECTOR, NATIONAL COMMITTEE AGAINST DISCRIMINATION IN HOUSING

Mr. SLOANE. Thank you, Mr. Chairman.

I am going to be very brief. I say amen to everything that my colleagues have said. We at the National Committee Against Discrimination in Housing believe that savings and loans and mutual savings banks are well worth saving, so long as they contribute to the public good. They have done so over a period of many, many years, and the Federal Government has been a major benefactor to these institutions. We believe these institutions have been of extraordinary benefit to the home seeking public and that Federal support has been worth it.

The reason I am going to be brief is that the main thing I would like to do is give you the perspective of my organization on this problem. NCDH is a fair housing organization which has been around for 32 years, dedicated to promoting fair housing and equal housing opportunity, including home ownership for racial and ethnic minorities, and for women. I want to address myself only to two particular aspects of the problem we are facing right now.

It has to do with adjustable rate mortgages and our concern is particularly two-fold, one, the variable rate mortgage, and second, negative amortization, both of which have been approved for implementation. Let me explain why we are concerned about that.

It has only been in recent years that minorities and women, largely through equal employment laws and the like, have achieved the economic position necessary to enable substantial numbers of them to participate at all in the mortgage market. Progress has been very slow, and they are still at the lowest end of the mortgage market. Under adjustable rate mortgages particularly variable rate mortgages, lenders must necessarily look at the ability of applicants to pay higher monthly payments than initially required. Thus, it is likely that this will drive minorities and women, currently at the lowest end of the mortgage market, out of it entirely, and place them back in their previous position of non mortgage market participants.

In addition, we are faced with the problem of stereotypes entertained by many mortgage lenders. Although once traditional stereotype notions of minorities and women as unreliable and unlikely to maintain stable jobs and steady income has been largely dispelled, other stereotypes persist, and are likely to foreclose them from the mortgage market under a system of adjustable rate mortgages.

What I mean is that mortgage lenders now recognize that minorities and women more or less can be counted on to hold stable jobs and maintain stable incomes over the period of the mortgage loan. Under fixed rate mortgages, they qualify for mortgage loans, and are perceived as being able to handle the equal monthly payments over the life of the loan.

By contrast, under adjustable rate mortgages, mortgage lenders must be able to see potential increased income, and are likely to approve loans only to applicants who they believe are upwardly mobile economically. Minorities and women do not fit into this category of borrowers under stereotyped notions that persist. Accordingly, they are likely to be rejected for adjustable rate mortgages.

The second problem, involves negative amortization. Under this method, mortgage lenders must count on appreciation of property values. In the past, mortgage lenders maintained the stereotype notion that houses in minority or racially integrated neighborhoods were likely to experience property value decline. Although this stereotype has been dispelled, at least in part, lenders do not generally accept the idea that property values in minority or racially integrated areas will increase nearly as rapidly as in all-white neighborhoods. Accordingly, they are less likely to make negative amortization loans in minority or racially integrated neighborhoods as in white neighborhoods.

What this means is that racial redlining, that incidious practice inflicted on many parts of our cities, is likely to recur.

Mr. Chairman, I have tried to be brief. I will stop right there. Our basic conclusion is that if we are to have adjustable rate mortgages there must be careful safeguards and controls to assure against the exacerbation of problems of race and sex discrimination.

Chairman Gonzalez. Thank you very much, Mr. Sloane.

Right off the bat, let me say that I personally deeply appreciate your presence and the thrust of your presentation. As you know, the last effort along the line of ameliorating discrimination in housing was the bill that we had in the prior Congress.

Mr. Sloane. I am very familiar with that, Mr. Chairman. I spent half my life on that bill.

Chairman Gonzalez. And I support it, of course, in the House, and got quite a bit of flak. The strongest flak came from the group that was here testifying yesterday on the current emergency on housing, so that I can appreciate very much what you are saying.

Do you find that your thinking would reach the point of recommending what I call the Adam Clayton Powell amendment? Years ago, before the Civil Rights Act, we would always have the Powell amendment. With the passage of the 1964 Civil Rights Act and section 7, that was really codified, but do you feel that there is some need to tailor something along those lines for this particular vehicle?

Mr. Sloane. I don't think any special fair housing safeguards are needed in this bill. We already have adequate fair housing safeguards under title VIII and other civil rights laws, particularly administrative enforcement. Title VIII is a weak vehicle in terms of enforcement. That is really what we were trying to do in trying to pass fair housing amendments legislation in 1980. The House, God bless you, passed it, and we almost made it in the Senate, but not quite. Lack of adequate enforcement remains the major problem.

The courts, as you may know, Mr. Chairman, have been very generous in their interpretation and construction of title VIII, but enforcement is still weak and the courts can do little about that. The Justice Department, as you may know, until about 2 weeks ago, had not filed a single suit under the fair housing law since the Reagan administration came in. That means that reliance has to be on administrative complaints with HUD, which has no enforcement power, or private enforcement, which is what NCDH do.

But let me explain. We have a staff of four lawyers at the National Committee Against Discrimination in Housing. Yet we represent the largest single private fair housing enforcement agency in the entire country. Four lawyers. The Justice Department has much, much more in the way fair housing enforcement resources. Yet they filed not a single suit until about 2 weeks ago, and then it was a very minor one.

We need administrative enforcement of title VIII. I don't think that Mr. St Germain's bill needs any additional civil rights safeguards. I think they are there. It is enforcement that we need.

Chairman GONZALEZ. Thank you very much, and God bless you for your endeavors.

I don't think Americans or any human being, for that matter, could really feel the sting of discrimination, whether it is racial, ethnic, religious, or economic, for that matter, who really hasn't confronted it or experienced it. It is so devastating and so impairing, particularly to our democratic society, that I consider that a number one challenge, particularly since the astounding statement and action by the President with respect to the tax exemption of private schools, where a President, a leader, says to Congress, we ought to have a law from the Congress when the law is on the books, as you pointed out.

Mr. SLOANE. You are absolutely right. What the administration has done on that is absolutely illegal. The courts have ruled on that. But I will tell you, the administration is not going to win on that one.

Chairman GONZALEZ. Well, I really salute your endeavor in that respect, because I do know how difficult it is to get either local, State, or national enforcement, even when the law finally was passed.

My time has expired.

Mr. Wortley?

Mr. WORTLEY. Thank you, Mr. Chairman.

I would like to get the reaction of the rest of you folks to a choice of enacting a capital assistance program for the thrifts or the regulators bill. Do you have any observations on that? We have already heard Mr. Brown's response.

Ms. CINCOTTA. I have no faith in the regulators at all. Before Jay Janis went out as head of the Federal Home Loan Bank Board, he said, don't look to us for mortgages. Look to the pension funds. He said it at a conference, in front of 500 people. When you touch the pension funds, our Governor says, we want it for reindustrialization. I don't have any faith in them. I am sorry. They haven't even come up with the home mortgage disclosure data that has been debated in Congress forever and passed, and we still don't have that information. We don't even have it from them.

Mr. **Wortley**. That isn't what I was asking about. I was asking how you felt about the regulators bill versus the capital infusion into the thrift industry.

Ms. **Cincotta**. I don't understand enough about it to answer that. I can get it to you.

Mr. **Wortley**. Mr. Sloane?

Mr. **Sloane**. I don't, either. I think John Brown does.

Mr. **Wortley**. Mr. Sisson?

Mr. **Sisson**. Well, I don't know. These regulators that are presently in place now, but I have known Chairman St Germain for 10 years, and I don't know these regulators, and I would go with anything he does. The thing I like about what he does, he says they are going to pay it back with interest.

Mr. **Wortley**. Mr. Brown?

Mr. **Brown**. I have thought a little more about that question since you asked it. Just to clarify the different aproaches between the two. With the regulators bill, the approach would be, as we point out in our testimony, primary reliance on supervisory mergers. With the capital infusion bill, there would be an effort made to keep some institutions alive with capital infusions and not merge them.

But as I said before, we don't see that the capital infusion bill in its present form has the type of requirements that would keep S. & L.'s making the type of lending that we want. But, putting that aside, just looking at the two bills as is, with the regulators bill, I think you would find a rapid homogenization of the banking system. With the capital infusion bill, I think there still would be homogenization. It just would not occur quite as fast.

But it is important to remember that most of the mergers, at least within the savings and loan industry, have been voluntary mergers. They have been occurring anyway.

Mr. **Wortley**. Voluntary mergers?

Mr. **Brown**. Yes. Last year, there were——

Mr. **Wortley**. A lot of them are pretty forced, from this vantage point.

Mr. **Brown**. I think the great preponderance of them have still been voluntary mergers between reasonably healthy institutions, to date. That could change very quickly.

One last thing, in terms of the cost. It is virtually impossible to calculate the relative cost of these two alternative approaches, because to do that requires assumptions about the future course of interest rates. If interest rates actually are much higher in future years than we expect or hope, then I think the capital infusion program could cost more, because you would be guaranteeing institutions and they wouldn't survive if interest rates went up.

On the other hand, if interest rates come down, as the advocates of Reaganomics hope, then the capital infusion program could cost less. But it is very speculative to argue very strenuously that one would cost that much more than the other.

Mr. **Wortley**. Thank you.

I wondered how the rest of the panelists feel about the elimination of the usury rate.

Ms. **Cincotta**. I think one of the things we have proposed is that there be an across-the-board usury rate. The problem when there were just the States' usury rates, with the fluctuation, money would flow to wherever you could get the highest interest, but with the removal of the usury rates the interest on all types of loans is just out of bounds, with no controls at all. So we would favor an across-the-board usury rate that the Congress could set.

Mr. **Wortley**. Thank you.

Mr. Sloane?

Mr. **Sloane**. I have nothing to add to what Ms. Cincotta said.

Mr. **Wortley**. Mr. Sisson?

Mr. **Sisson**. Same with me. I will stay with Ms. Cincotta's statement.

Mr. **Wortley**. Thank you.

Thank you, Mr. Chairman.

Chairman **Gonzalez**. Thank you, Mr. Wortley.

Mr. St Germain?

Mr. **St Germain**. I would like to answer your question, George. Mr. Wortley, I would like to answer your question.

Mr. **Wortley**. Fine.

Mr. **St Germain**. The regulators bill and the legislation before us today are two separate items entirely. I feel that we need both of them. It is not an either/or. If you will recall, one reason for the regulators bill was to preclude bank holding companies from buying up S. & L.'s. That was one of the primary purposes of my getting involved with that one, because I think that any day now you are going to see the Fed begin to, if not voluntarily, by court edict, begin to approve the bank holding company acquisitions of thrifts on an interstate basis. I don't think that is what we want, I really don't, because there goes the thrift industry, and if we hope that we can keep them in mortgage lending, certainly we can't keep them in mortgage lending if they are gone, and that is my concern.

So, what it indeed does, George, is to say, we, the Congress, are going to set the guidelines by which you effectuate mergers. If you recall, we debated it very, very thoroughly. The markup session, I thought, was an excellent one. Then on the floor we did quite well. However, that was back in October or November.

Now, we find that high interest rates have persisted. We get the Brookings Institution report, and no one denies that we have a great number of institutions out there that may well not survive for too long a period of time unless they get the type of assistance that is included in this legislation.

So, I don't think it is an either/or. The regulators bill was one step, a necessary step. I wish the Senate would act on it. This, I feel, is another emergency step. I really feel that this is emergency legislation that has to be addressed, and addressed promptly.

Mr. **Wortley**. Mr. Chairman, are you concerned about the possibility that we would infuse capital into some institutions and then ultimately they would fail, and we would still have to force a merger or pay it all off?

Mr. **St Germain**. George, I am happy you asked me that question. Certainly, you don't anticipate failures, because the President says things are going to get better.

Mr. **Wortley**. And they are.

Mr. **St Germain**. OK. So if they are going to get better, you give these institutions a little capital infusion to tide them over, and they have got it made in the shade. They will survive. They will be viable and they won't even have to draw down any funds.

Mr. **Wortley**. A healthier merger partner for the future.

Mr. **St Germain**. Well, if indeed—you see, Jonathan was right about the mergers. There have been mergers going on on a constant basis, even prior to this long period of sustained high interest rates. They have been going on on a regular basis. It is an evolutionary thing. The family that started the S. & L.'s has gone through three generations, and all of a sudden they don't have sons, just daughters, and those daughters marry doctors, so there is nobody around to run the S. & L.'s, so they merge it. You see, that has been going on for a long time.

Mr. Sisson, I am sorry you could not be here this morning. We had a witness here this morning who was very impressive, and frankly, he was sort of like the littlest guy here. His name was William Muse, Jr., president, Imperial Savings & Loan, from Martinsville, Va., and he was representing the American Savings & Loan League, and he stated:

> The ASSL members are savings associations owned or controlled by blacks, Hispanics, and Asian Americans. Our associations are small. They are young. Most of us have less than $100 million in assets, and only one-half have been in existence for more than 10 years.

Now, he submitted a four-page statement. He didn't ask for anything extra, or any changes. He didn't ask us to loosen up on the requirements, as some others did. He was very forthright. All he said was:

> We support the Home Mortgage Credit Capital Stability Act because it is a timely remedy for the thrift industry as a whole. Moreover, we have a particular desire to see the bill passed for the assistance is not partial to big associations, but is committed to save any viable mortgage lending depository institution, regardless of its size, if it meets the criteria. This would assure that the standard of fairness is maintained, and would have the added benefit of preserving the separate identity of the minority S. & L.'s, whether governmental assistance will come in the form of capital stability funds, net worth guarantees, or some combination of the two, it will be a long overdue measure to relieve the burdens of our industry. Therefore, the American Savings & Loan League supports this proposal and would urge its speedy enactment.

Mr. **Sisson**. Well, I say, God bless him, and I would sure like to have you give me his name and address so I could send him our statement to see his reaction to it, because I think our position on this is geared toward that type of an S. & L.

Mr. **St Germain**. Hall, let me ask you this question. Do you think, is it your opinion that absent the amendments you seek, we should not adopt any legislation at this time?

Mr. **Sisson**. No, no. Our basic premise is, you have to save the industry. Like I said, we have to do something about it, but what we are saying is that——

Mr. **St Germain**. You would like it improved.

Mr. **Sisson**. Yes. This is a golden opportunity for you all to make a clear demonstration to the financial community as a whole that we have an obligation in this country to have a certain type of institution, whether you want to call it a full service bank or an S. & L. or a savings bank or whatever you want to call it that will provide the money for home mortgages, and just not let these people turn their backs on the American public.

I mean, I despair of the fact that the people I represent, and these are primarily young men and women out of high school, their first job in the small town is with the telephone company. That is where you make the most money in the small towns in the South or Southwest or even in West Virginia, where this gentleman is from, and those people now are abandoning the hope of ever owning a home. That part of the American dream is fast dying away.

I mean, they may have to go back and move in with mom and pop, but they are never going to go out and buy their own home.

Mr. **St Germain**. You know, you are carrying coals to Newcastle.

Mr. **Sisson**. I know I am carrying coals to Newcastle, but it is kind of cathartic to say it once in a while anyhow.

Mr. **St Germain**. Now, you know, the real fight on all of this frankly—and this is my point—the real fight is going to come when and if the day arrives that from the other body comes the Orient Express. It will make the Orient Express look like a Toonerville Trolley, because they are going to have that loaded down with so much. They are going to attempt to eliminate a lot of the gains that we made to date, and that is where the big fight is going to come.

Mr. **Sisson**. Well, you know we have been very effective, this group here, Mr. Chairman, in that every other month we side with the other faction, you see, and then immediately this tenuous agreement that has been built up suddenly collapses. So I can go home to my wife at night and say that I am a very effective lobbyist because I have kept that bill from coming out of the Senate Banking Committee.

Mr. **St Germain**. Well, hopefully this committee can proceed with its hearings on the FIRE document and come up with something meaningful and constructive and well thought out and not just a conglomeration of wish lists.

Mr. **Sisson**. I think you had better hurry, Mr. Chairman, because if I read my newspaper correctly this morning, the deal seems to be getting cut over there about subsidizing mortgages and that sort of thing.

Mr. **St Germain**. Thank you, Mr. Chairman.

Chairman **Gonzalez**. Thank you.

Mr. Schumer.

Mr. **Schumer**. Thank you, Mr. Chairman.

First, I was interested to hear Mr. Sisson describe CWA members as young and mobile and newly married. That does not describe my mother-in-law, and she is a CWA member.

Mr. **Sisson**. Your mother-in-law is the backbone of CWA.

Mr. **Schumer**. She is on my back all the time, too.

[Laughter.]

Mr. **Schumer**. Until I was married, which was only 1 year ago, I never understood all of these mother-in-law jokes, and now I understand them very well.

I just would like to open this up to the whole panel and just play a little bit with your 50-percent idea which I am intrigued with and I think is a good one.

Well, let me pose for you two hypotheticals, and I would like to get all of your judgments on it. One, if you are saying we should put limits on the variable rate mortgage, which as I told you I have a great deal of sympathy with but I also have some trouble with, but that it is countervailed or counterbalanced by the fact that only 50 percent of the portfolio be that and the other 50 percent can be all of these fat income-producing things.

What about an 80-percent requirement or a 90-percent requirement but let the rate float exactly with or closer to the actual going mortgage rate? Thereby you are getting more money into housing, but at the same time the average consumer is going to pay more if interest rates continue to go up.

You see, it is my belief that if interest rates continue to go up another 10 or 20 percent from what they are now, our country is gone and all these questions are trivial anyway. What would be your judgment on that? And then let me pose the opposite hypothetical.

What about if we took Mr. Garn's approach and we allowed everybody to do everything at once, let every financial institution, whether it be the First Decinel of Peoria or Chase Manhattan or Merrill Lynch or Sears, Roebuck, if they got into it, would have to put a certain percentage, a set percentage of their money into mortgages—10 percent, 20 percent, something so there would be enough mortgage money floating around.

Those are two things that I am not sure I support. I probably do not support either of them, but I would like to just get your judgment on it, why they would be bad or why not.

Ms. CINCOTTA. The problem that you have now is with the interest rates as they are, people cannot afford—I think the data that I was talking about, the high foreclosures already, all of the type of creative financing, owner financing, people just cannot afford it. People are sitting there like with a timebomb even waiting for those, the balloons to pop; that I do not know how people can afford it.

Mr. SCHUMER. Right. But basically I mean I understand that. That is a problem with high interest rates. That is really not the problem we are addressing here, because even by your plan there would be a lag, but the interest rates would go to that level, so that is a different problem. The high interest rates cause both.

The problem of an average working family, or these days an upper middle class income family not being able to afford a home, that is not what the problem is that we are talking about.

Ms. CINCOTTA. The part that intrigued us about the S. & L. League proposal is that there would be the write-down on the mortgages, and they would probably come out at 10 to 12 percent, and that infusion of capital at that percentage mortgage now would make a lot of difference right now. And if you put a cap on how high they could go up, you would have a sum of money that would be at an affordable rate.

Mr. SCHUMER. But in the joint statement you did not propose that?

Ms. CINCOTTA. I did not sign the joint statement.

Mr. SCHUMER. Well, then this may be addressed to the other joint statement signers.

Mr. **Brown**. If I could address that. Your question hits directly at the most difficult issue that we had to resolve in preparing the joint statement. There clearly is a tradeoff. Savings and loans can only absorb so much interest rate risk. You can ask them to have a higher proportion of their portfolio in mortgages if those mortgages are more volatile. In other words, they could have 80 or 90 percent of their portfolio in mortgages if they were free-floating mortgages. If they are fixed rate mortgages, in order to be prudent that percentage has to be much lower, maybe as low as 20 percent or even lower.

So recognizing that we had to strike a balance, our feeling was that it was more important to have a portfolio requirement that emphasized the quality of the mortgages in terms of having limits on the volatility than it was to have just a gross mortgage portfolio requirement that did not emphasize restraints on rate increases.

And the reasons for that were really twofold. One is that in having a portfolio requirement that focuses on the quality of the mortgages—in other words, limiting the rate increases—you are guaranteeing at least some supply of mortgages of that type. I think just their presence in the market will prevent the type of total transition to the more volatile ones which has occurred in places like Canada. There is a lot of peer pressure in the market, and consumers could see that at least somewhere at some time they could get an adjustable rate mortgage with safeguards.

Mr. **Schumer**. It is kind of like decontrol on gas and oil.

Mr. **Brown**. It is going to put pressure on other lenders in the market to adopt some similar standards or at least move in that direction.

The second point was that we felt that it is very important to be realistic. You have to recognize that savings and loans are not going to be the end-all primary source of mortgage credit in the future that they have been in the past. The mortgage market is changing. The secondary market is growing. The pension funds have got to become involved. So we have to look to other mortgage sources. Therefore, we see that although you can make a case that if the savings and loans' aggregate mortgage portfolio falls from 80 percent to 60 percent, you are losing mortgages; that probably will not have a major impact on the overall supply factor. So we shifted our emphasis to the quality part, in other words, the safeguard aspect.

And the last response is that we are not saying that savings and loans can only make mortgages with these safeguards. We are just simply saying that 50 percent of their portfolio should have these safeguards. They would be perfectly free to go above that.

Mr. **Schumer**. Could you do some kind of mathematical balancing? I mean a two-thirds float is 50 percent, and a three-quarters would have been 70 percent or any of these.

If I could again, since you have to send me something else, if you could send me the components that went into that, I would appreciate it.

Mr. **Brown**. I would be glad to.

Mr. **Schumer**. What about the other proposal which is probably off the wall, but I figured I would like your comments or Mr. Sisson's, the defenders of mothers-in-law. [Laughter.]

Mr. SISSON. I have to admit that I never thought I would join the banks or the S. & L.'s, but I do not think Sears should be—I think Sears should be selling fertilizer and garden tractors and blue jeans instead of getting into the hot money market. And I think that one of these days Chairman St Germain and all of you are going to have to face the problems of the money funds and the Sears and all of these people, because this is going to be a real problem for our country one of these days.

Mr. SCHUMER. Do you agree with that, Mr. Brown?

Mr. BROWN. We have not really taken a formal position. I am speaking as an individual organization, the Ralph Nader organization as opposed to the full coalition. The reason the coalition did not address that was simply that the legislation deals with the savings and loan industry, and we felt that——

Mr. SCHUMER. I do not support it myself.

Mr. BROWN. We saw the chairman's concern with some of our proposals. I think if we had gone that further step, then there would have been even more concern about the tactical possibility of the proposals. But I just think we have to reserve judgment on that.

Mr. SCHUMER. You are basically in collaboration with that, Ms. Cincotta, or not? And I know, Mr. Sloane, it is not your area.

Mr. SLOANE. It is not my area of expertise.

Ms. CINCOTTA. I think that some of us represent different constituencies. I think that our constituency is not middle class, not necessarily upwardly mobile, and we just have very deep concerns for any kind of renegotiable mortgage, what Merrill Lynch is doing, what the money market funds. We just do not see that there is going to be an industry that is going to provide housing at affordable cost.

If the bill that was offered here today had a write-down or a buydown plan, we would have supported that because that would have led directly to some immediate aid to the consumer for at least 3 years, and hopefully with all of our work, interest rates would come down.

But our fear is with all of the stuff that has been going on with the money market, everything, there is not going to be a place for housing. And if the S. & L.'s—you know, when you go and talk to them in their office and they say we are going to write insurance and we are going to do this, and unless they are saved for what they are good for, they are good for mortgages. We support that. We have supported that in the past. We have told them that pretty soon there is not going to be anything to save. It will be like saving a bank who does not write mortgages or something.

But there has got to be something in there for the consumer, and there has got to be some place that people can get mortgages. The S. & L.'s right up to this point seem to be that best place. And there have got to be some safeguards on the adjustable rate mortgages. It just does not—people cannot afford it.

Mr. SISSON. Mr. Schumer, just to go back a minute, I remember, I guess it was almost 20 years ago when American Express got in the salad oil business, and you remember what happened then.

Mr. SCHUMER. That 20-year period seems to be the domain of my two respective chairmen, so I will ask them what happened.

I think I had better yield back the rest of my time. [Laughter.]

Chairman **Gonzalez**. Just one question to the distinguished gentleman from New York, and that is, did I hear him say that he was in favor of the 50-percent mandate or proviso?

Mr. **Schumer**. That I did not favor it? No. I was just trying to understand how they came up with 50 percent and a two-thirds rate rise as opposed to an 80 percent and a full rate rise or a 20 percent and a quarter rate rise.

But just one other point that I would mention is again I am very worried about what would happen in a conference. I mean when you see the stuff that they want to throw on bills over there it might make all of us wish we had not done any of this unless it is handled as carefully as possible.

Chairman **Gonzalez**. Well, we cannot control that. But the reason I was asking was because if the gentleman had signified his opposition, I was going to offer a trade here. We would not send a copy of this transcript to your mother-in-law. [Laughter.]

Mr. Hoyer has indicated he does not have any questions, but maybe he has a statement. Certainly we would recognize you, Mr. Hoyer.

Mr. **Hoyer**. I would just like to say that I thought the statements were excellent, and I am in the process of learning about all of these great things. I am, as you know, new to the Congress, and I am not an expert like Mr. Schumer who has been working on this pretty hard.

It is obviously a tremendously difficult problem, and I do share Mr. Schumer's view. We have two bills here, two major bills. They both are working very hard to try to come up with something that will fly on both sides, because we saw full well how in one of the first major pieces of legislation I voted on, the regulators bill, that of course nothing happened on that side. So this seems to be my impression of why we are working from somewhat more simplified terms.

Thank you, Mr. Chairman.

Chairman **Gonzalez**. Thank you, Mr. Hoyer.

Mr. Wortley, we will go into round No. 2 here. I am sure you are waiting because you have a question to followup.

Mr. **Wortley**. Yes. I would just like to ask Mr. Sisson, does your union pension fund have any money invested in mortgages?

Mr. **Sisson**. Unfortunately or fortunately we have absolutely no control over our union pension fund. It is run entirely by American Telephone & Telegraph, and every 3 years when we go into the collective bargaining posture with them we have to negotiate pension benefits out of that pension fund. No one from CWA sits on the board. No one advises them about where they should invest their money.

Now, that may change in later years, and in fact, I know that there is supposedly a group forming at the AFL–CIO to discuss the possibility of unions like the carpenters, who have a large pension fund, putting some of it into home mortgages.

Mr. **Wortley**. I am surprised a progressive union like your own does not have some sort of say where that money is invested.

Mr. **Sisson**. Well, you see, the pension fund started way back in the early 1900's. CWA only came around right after the Second

World War, and by that time it was so large and concrete we did not have a chance to get in on it. It is a very old pension fund, and it has got untold billions of dollars in it.

Mr. **Wortley**. Maybe we should defer this for next week when we have another witness on behalf of the AFL-CIO, but do you have any ideas, any thoughts at all on how much of the union's pension funds are invested in housing in this country?

Mr. **Sisson**. No, I do not, and I think Henry Schechter is the one to ask that, because he is the head of the Housing Department, and he will know. He can give you a very good idea of how much money they have in housing.

Mr. **Wortley**. Thank you very much.

I yield back the balance of my time.

Mr. **St Germain**. The answer to that one, George, is not enough, much too little.

Mr. **Hoyer**. Would the gentleman yield?

I would like to make just one brief observation following that question. I do not know whether the gentleman saw it, but the State of Maryland Employee Pension Fund has just put $20 million into home mortgages. This is the first State pension fund, as I understand it, in the United States to have taken such action and perhaps it will be a forerunner for many States to follow.

Mr. **Wortley**. A progressive State, of course.

Mr. **Hoyer**. Of course.

Chairman **Gonzalez**. Let me add something to that. A whole year ago I had advanced a suggestion and found reception from California. A fellow Congressman brought in two very eminent experts, one a State assemblyman from California and the other a lawyer expert in the investment area. And at that time the problem was that in order to draw in pension fund source money into such things as mortgages where you would have some opportunity to legally do so for periods beyond say 5 years, even as short as 7 or 7½ years, they had to first seek an amendment in California law soon to make it possible to tap that source. They were successful in obtaining this change.

By the time we went on the subcommittee visit in January, the first week of January this year, there were better than $2 billion that had been grown into that type of investment from this source nationally since—it will be 2 years—well, it was right before the Carter administration went out.

The AFL-CIO construction labor unions met, and I met with Secretary Marshall in order to seek administrative changes that would allow some diversion of those funds, and they did. We did obtain it to the extent we could. The big question, and I think it is still a question, is to what extent we would have to have some statutory enactment—I think that is the remaining question—in order to trigger. And we also have to provide a mechanism whereby we can draw this source, which I think is a tremendous area, and utilize it in this particular area with the observation of the protective laws in your long-term mortgage.

And we thought that we could have a revival of some features of FHA mechanism to harness it in in tandem with some statutory changes that would allow short-term extension of short-term provisos.

I do want to say that this is an area. I think California was the first State that really went in heavily, but Maryland also has pioneered. So I thought I would add that for the record.

Mr. **Wortley**. Mr. Chairman, before we conclude the discussion could we just correct the record? I think it ws Mr. Sisson who was referring to American Express being involved in a rather exotic investment scheme. I would not want to damage American Express, but I do not think it was American Express that you are referring to. Was it not in fact Atlantic Express rather than American Express?

Mr. **Sisson**. No, Mr. Wortley. I was working on Wall Street at the time when the salad oil scandal broke, and it was the American Express Co., because everybody was wondering how come a credit card company was getting involved in buying all of the salad oil over in New Jersey, and the tanks were empty.

Mr. **Wortley**. It was American Express?

Mr. **Sisson**. Yes, sir.

Chairman **Gonzalez**. Mr. St Germain.

Mr. **St Germain**. May I make an observation with respect to the pension funds?

George, I do not know if your staff had an opportunity to bring to your attention the questionnaire from the homebuilders. Did you happen to glance at that?

Mr. **Wortley**. Yes, I did.

Mr. **St Germain**. And you will notice there were a couple of questions there: Would you support statutory changes that would allow or would assist pension fund money to be invested in housing, and do you support regulatory changes? So there is a requirement for both regulatory and statutory changes in various areas.

You know the prudent man rule and things like that. I think labor has jurisdiction, the Department of Labor, that some regulatory change had to be made there, and———

Mr. **Wortley**. I replied affirmatively on both of those questions.

Mr. **St Germain**. Thank you, Mr. Chairman. And I would like to thank the panel for a very stimulating and very valuable exchange as well as their testimony and their submissions.

Chairman **Gonzalez**. Mr. Hoyer, I think you indicated you either had a question or not?

Mr. **Hoyer**. No, Mr. Chairman.

Chairman **Gonzalez**. Well, if there are no further questions, I would join the full committee chairman in thanking the panelists for a very fruitful contribution, and always coming from the people—I call it the cutting edge—it is most helpful.

We thank you, and we will hope to continue a communication and dialog with you. Thank you again.

The subcommittee will stand in adjournment until Tuesday next—I think that is March 23—at 9:30 a.m.

[Whereupon, at 4:20 p.m., the hearing was adjourned, to be reconvened at 9:30 a.m., Tuesday, March 23, 1982.]

HOUSING AND URBAN-RURAL RECOVERY ACT OF 1982

TUESDAY, MARCH 23, 1982

House of Representatives,
Committee on Banking, Finance and Urban Affairs,
Subcommittee on Housing and Community Development,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:35 a.m., in room 2220, Rayburn House Office Building; Hon. Henry B. Gonzalez (chairman of the subcommittee) presiding.

Present: Representatives Gonzalez, St Germain LaFalce, Vento, Mitchell, Schumer, Frank, Stanton, Evans, Wortley, Carman, and Lowery.

Also present: Congressman Frederick W. Richmond.

Chairman **Gonzalez**. The subcommittee will please come to order.

Mr. Mitchell, thank you very much for your presence.

The subcommittee will continue the hearings initiated last week. I am delighted that we have the commissioner of housing and community renewal of the great State of New York as our leadoff witness, and I am going to ask our distinguished New York colleague, Mr. LaFalce, to introduce him.

Mr. **LaFalce**. We say good things both about the city of New York and the State of New York. It is just that we say better things about upstate than downstate.

It is a real pleasure to have Mr. Berman here. He has been commissioner for little over 1 year now, and has developed an outstanding reputation during that period of time, and I don't think we have to be long-winded or flowery about it. I think we should hear from Mr. Berman and his assistant, so why don't we do that, Mr. Chairman?

Chairman **Gonzalez**. That is fine, except for the fact that I noticed that Congressman Richmond is present and I gather that Mr. Berman might be his constituent.

May I ask where you do vote, Mr. Berman?

Mr. **Berman**. As long as you don't ask me how I vote.

Mr. **LaFalce**. As long as you don't live in New Jersey.

Mr. **Berman**. I live in Westchester.

Mr. **LaFalce**. That would be Mr. Ottinger's or Mr. Peyser's district?

Mr. **Berman**. Mr. Ottinger.

Chairman **Gonzalez**. Sam Stratton's old district?

Mr. **Berman**. No.

Chairman **Gonzalez**. Well, we are very honored to have our colleague, Mr. Richmond. I know that Fred isn't a member of the committee, but I have always found him to be so responsive to our needs. It is a pleasure.

Mr. **LaFalce**. I think we can give Mr. Richmond a better introduction than that. He is also well known as Mayor Koch's chief adviser on rural America. [General laughter.]

Chairman **Gonzalez**. That is very important.

Mr. **Richmond**. Mr. Chairman, I just stopped in this morning to help welcome Mr. Berman, who I consider to be among the finest executives we have in New York State. Every job that Mr Berman has ever handled, he has handled beautifully. I am proud to have him as one of our State officials, and I am proud to welcome him.

Chairman **Gonzalez**. Thank you very, very much.

Mr. **Richmond**. He is also my friend.

Chairman **Gonzalez**. Now we have Mr. Wortley. What happened to you? You didn't get into a redistricting fight, did you? [General laughter.]

Mr. **Wortley**. Someone was twisting my arm.

Chairman **Gonzalez**. Well, if President Johnson were around, I wouldn't even ask, but that is something. It must have been Stockman. [General laughter.]

If you have a statement, we certainly recognize you, Mr. Wortley, for any purpose.

Mr. **Wortley**. I have no statement. I welcome Mr. Berman. It is nice to have authorities from New York City come down and straighten out Washington, D.C.

Chairman **Gonzalez**. Well, all right.

Well, Mr. Berman, you may proceed as you see fit. We want to thank you for your prepared statement that we have had ample time to examine. We are always very grateful for that. If you wish to offer the prepared text for the record, we can proceed and then you may summarize it; it is your choice.

STATEMENT OF HON. RICHARD A. BERMAN, COMMISSIONER OF HOUSING AND COMMUNITY RENEWAL, NEW YORK STATE, ACCOMPANIED BY SYDELLE KNEPPER, ASSISTANT COMMISSIONER FOR DEVELOPMENT

Mr. **Berman**. Mr. Chairman and distinguished members and friends from New York, one is, I want to thank you for having me here, and No. 2 is, I would like to introduce my coworker, Sydelle Knepper, who is the assistant commissioner for development for the Division of Housing.

Then, what I would like to do is submit the text for the record, and just try to highlight a couple of areas before I do what is probably more meaningful for you, which is to take your questions.

Chairman **Gonzalez**. Without objection, so ordered.

Mr. **Berman**. Let me begin by saying it is a real pleasure to be here to comment specifically on your housing plan, H.R. 5731, and on behalf of Governor Carey and the people of New York. We hope that some of our comments will be helpful to you as you continue to promote legislation which meets the needs of millions of New Yorkers.

I would also like to specially thank colleagues from New York for their welcome and their continued support for both me personally and the work that needs to be done. They have been doing so well here in keeping the issues of both health and housing on top of the national agenda, and especially Congressman Mitchell, who quickly will see that we have lifted a lot of his material. It is not easy for you Congressmen to continue your efforts to keep housing on top, so we hope we will give you some more facts and some more issues to support you.

We from New York want to recognize you for taking a very difficult task in a very difficult environment, and keeping housing on the agenda, and more importantly, a problem that has to be dealt with. It is probably even more difficult because there is no Federal housing policy. There has not been an articulation of a national housing policy or strategy, and therefore it is hard to measure how well you are progressing, or if any particular proposal gets you closer or further from your goal.

What I would like to say is that, there are clearly the social and important human issues of housing, but I also want to reiterate the fact that if you look at the history, there has never been a time that we have had a healthy economy in this country back as far as 1900 where we have not had at the same time a healthy housing construction industry. It is not unusual that strong housing programs have been used as the stimulation or the lynchpin in economic recovery.

So, I would urge you to not only let housing be seen as the important issue which it is, but also as part of any economic stimulation package.

I have taken the liberty, and it has probably been a bit presumptious to describe what I think a housing goal ought to be, and I want to state it so that you know the backdrop from which I am trying to evaluate the different proposals and to make recommendations.

It seems to me our national housing policy ought to be to assure safe, suitable, and affordable housing in viable communities with equal access for all. I don't want to dwell on it, but if you look at the three major issues, and I have provided them in the text, you will see that we have a lack of affordable housing, a lack of adequate, suitable housing, and a lack of equal access to housing.

This problem is at a crisis level. The problem is not isolated in our inner cities. It is not restricted to our suburbs. It applies to rural New York as well. The nature and the degree of the problem has now reached magnitudes that if they occurred in any other sector of the economy we would have taken immediate emergency action to try to put our thumb in the dike, if nothing else.

When you find that the number of homeless in the State of New York has been estimated by some to be as high as the entire population of Santa Fe, when you find that there are over 6 million people nationally who are living in what has already been identified by HUD to be substandard housing, and another 2 million living in overcrowded conditions, when you find that 71 percent of the elderly in New York City pay more than 25 percent of their income for rent, no matter what indicators you go to, the severity of the problem, the nature of the problem is clear.

And so, rather than dwell on that, what I would like to do is to propose four strategies for improvement. The first is to provide financial assistance to those who cannot afford suitable housing. The second is to provide for national incentives for the private sector to increase supply in order to provide housing for those who cannot secure it in the pure market economy.

The third is to strengthen and revitalize our neighborhoods and renew investment in communities, and the fourth is to establish programs to assure equal opportunity and accessibility for particularly minorities.

What I have then tried to do, and I will ask you to go to page 7 in the prepared remarks, was to begin to compare the administration's proposals and your proposals in each of these four strategy areas.

The first is to provide for national assistance to keep housing affordable. The bottom line, as you look at page 7, is clear, that people without money need to be housed and they can't do it without money. Rhetoric will not substitute for money. Turning our back on the situation or reducing its financing does not solve it. As you look down here, what you see is, again, not solving the problem or a failure to solve the problem in the President's proposals, and a much more healthy direction in terms of H.R. 5731.

I would offer three additional recommendations to you. The first is on the emergency mortgage relief program I think you will do better to have the States target the funds in a bit more of an effort than we currently have with HUD targeting the funds. I think your State people can have a sense and do have a sense of where the needs are. We are working with neighborhood conservation groups. It is as important a program for upstate as it is in our situation, as it is for the suburbs, as it is for the central cities, and I think the States are in the best position to make that determination, not to fund the program, but to make the allocation decisions.

Again, on the section 8 existing program, the State set-aside, I think, is a crucial element for the nonentitled communities. We have a situation where if you are a non-entitled community, even though we administer the program and find a subcontractor in the local area to actually administer the program, the State has very little, if any, input into the priorities for that funding within the State.

So, as a State policy, we would want to assure that as much of the need is met in rural areas, in suburbia, in central cities, and we all look to a balance. We do not have input in the current existing section 8.

We would also urge this committee to try to do a bit more with the welfare rent subsidies and the relationship between HUD and HHS. It is clear to me that when the largest subsidy program that is run in terms of housing is through welfare rent, and in terms of assuring that those people are living in standard housing and in the area of priority and in the area of availability, it turns out to be an important and crucial area which I think the States could help. I also think the Housing Subcommittee should have a large influence over funding because it is too basic an issue for it to be considered strictly as part of the HHS budget.

Let me move on to strategy two, which again was to provide financial incentives to increase supply and availability. There is no question, again from even the HUD statistics, of the inadequacy of the current supply. What you see here are either blunt or disguised measures which would dry up sources of capital for housing. I want to reiterate that in the best of times, in the fifties, we had a healthy economy, we had low unemployment, we had interest rates below 6 percent, and yet there were communities where the private housing industry did not enter.

New York State had to develop the Mitchell-Lama program for moderate income people. New York State had to develop programs for the aged, for rural Americans and Indians. These are the groups of people usually left out of the marketplace. So for those of you counting on the turn in the economy to solve the problem, I don't think any of you have talked about unemployment at the rates they were in the fifties or interest rates as they were in the fifties. At that time, we had big gaps, so the drying up of the capital market is a poor strategy for housing and for economic recovery. Mr. Chairman, your approach is much more healthy.

Let me again try to, in a quick and succinct way, offer several suggestions or at least areas for consideration. Again, on the 312 program, I think it is worthy to consider the sliding interest rate, the targeting of funds and tighter administrative controls because there has been some problem with defaults, as I understand it.

More importantly, on the 312 program, it seemed to me that we have an opportunity to make some real impact with this program. It is a desirable program. It will probably fit upstate much better than some of our city areas, and again, we have been working with those areas. We know from our neighborhood preservation programs and some of our other work how it can be done.

The same with housing for elderly, the section 202 program; obviously, it needs to be strengthened. I would suggest that when we look at the data on the elderly, additional investment in that program is probably worthy, and we also favor the use of flexible subsidy funds, obviously both for federally and nonfederally insured projects. That is a little parochial, but if you think you have problems with your federally insured, let me reassure you that we also have problems with the programs not federally insured in New York.

Our 236 portfolio last year cost the State, in debt service payments and others, about $200 million.

So, again, I understand the need for that program. I would urge that rather than exchanging Federal for State dollars, to use the money for new programs and more housing.

The third is to revitalize our neighborhoods and community renewal. I think all of us, when we sit back and don't think of ourselves in the business of assisting housing, and think about how each of us goes about making our own housing decisions, we are willing to make a lot of compromises in the shape of house, size of house, the insides of a house, even the exterior of a house. But the first thing we shop for is neighborhoods, and important support services such as schools and convenience of commercial areas. Revitalizing a lot of our communities is such an integral part of housing that it seems to me it is crucial that we keep our emphasis in that area and not abandon it.

We obviously are supportive of the efforts some of our colleagues and you have made in terms of what I call the UDAG for housing. We are very concerned about the elimination of the low and moderate income family language and some of the accounting and recordkeeping that was proposed by the administration. I know that you have worked hard in trying to reach some agreement with the Secretary, but I think it is worth considering three other areas.

One is that as we talk about CDGB. It seems to me it is worthwhile for Congress to either ask or require that the States earmark an amount for rural, suburban, and inner-city. The problems of rural New York cities, villages, or towns are slightly different from those in the inner city, but yet the infrastructure in the rural areas, whether it is water, sewer, or whether it is basic highways and street lights, whether it is curbs and gutters, is as crucial to making those places proper places to live as some of our inner-city areas.

Right now, if you are not an entitlement city, the relationships are all with HUD, and it makes no sense. The other choice is better coordination between HUD and Farmers Home. There are a lot of exciting Farmers Home programs which you have restored in your bill. I can't emphasize enough how important the 515 rental assistance portion of the bill is. We have developers ready to go in rural New York, willing to build primarily for our elderly, projects under 50 units, and with the fixed incomes of the elderly, we are not able to make housing financially feasible, and therefore it is not being built.

The problems between HUD and Farmers Home on farm labor is a crucial problem. We are getting into these sorts of things because you can't build housing for seasonal workers. There is no financial liability in 3 months' occupancy. Therefore you can only build seasonal worker housing if it is occupied 12 months a year. That type of catch-22—I don't even want to call it catch-22, because there are no double digits in it, but catch-1 doesn't make any sense.

If we are interested in building substantial, adequate housing for our farm workers and for our seasonal workers, then you have to do it on those terms, and it seems to me that they have put up arbitrary roadblocks to assure that the funding will never be used.

Obviously, on the block grant, I think the neighborhood strategy areas requirements of citizen participation have added to the value, and not depleted the value.

The fourth area, which I will not dwell on too long, is the protection of rights of equal access in our minority areas. It is clear to me and it is clear if you look at the earlier part of the testimony that discrimination still exists and persists. We must provide a mechanism to enforce fair housing and to insure that minorities get their share of any public funds.

I am hopeful that maybe you will resurrect some of the legislation in H.R. 5200 that passed this House and make it part of your bill. But again, I understand the need perhaps to attack each of these strategies separately. I would just ask that you do attack it.

There are three other issues which I dealt with here in the paper that deal with rent control and the voucher program along with public housing, but I will hold those, and see if there are questions about it.

We in New York understand the need for fiscal restraint as well as fiscal responsibility. We are not down here pretending there is a well that is endless. We know that scarce resources have to be balanced with prudence and compassion. New York was able to avoid financial disaster and redesign its fiscal plan in line with fiscal realities. This was done equitably, without placing our most vulnerable residents in jeopardy.

If we are to assure our Nation's economic health, then this administration, like the New York State administration, must move housing and community development issues up on its agenda. New Federalism is not the answer. As the Governor said in the first year of the President's proposal, New Federalism means that New York State's local governments would have to absorb about $1 billion of withdrawal of Federal money.

The housing needs of our citizens will not disappear because we ignore them or stop funding them. Rhetoric won't solve this problem. Only money can do that. The development of a long-range housing policy requires the commitment and assurance of future funds. We cannot ask our brothers in the private sector to enter into this partnership of long-term financial relationship when government shows no interest in making such a commitment on its own. The Federal Government has a long history of acknowledging its responsibility in housing. I am very encouraged that this subcommittee, under your leadership, Mr. Chairman, is determined to maintain this national commitment, and I thank you.

[The prepared statement of Mr. Berman follows:]

NEW YORK STATE
DIVISION OF
**HOUSING AND
COMMUNITY
RENEWAL**

RICHARD A.
BERMAN
COMMISSIONER

TWO WORLD
TRADE CENTER
NEW YORK
NY 10047

212 488-4962

REMARKS

March 23, 1982

Richard A. Berman
Commissioner
New York State
Division of Housing and Community Renewal

before

Subcommittee on Housing and Community Development
U.S. House of Representatives
Washington, D.C.

Chairman Gonzalez and distinguished members of the Subcommittee, I am pleased to be here today to comment on the housing plan offered by the Administration and H.R. 5731 proposed by members of this subcommittee.

On behalf of Governor Carey and the people of New York State, I thank you for this opportunity. I hope our analysis will be helpful as you work to enact legislation needed to meet the housing needs of millions of Americans.

Our national housing program must be responsible, equitable and effective; it must contain provisions necessary to make the economy sound once again. The plan (H.R. 5731) devised by you, Mr. Chairman, with the help of your colleagues from the New York delegation, is an important first step in a successful attack on our housing crisis.

I believe there is a need for the federal government to articulate and promote a national housing goal. Central to the goal is a set of minimum basic strategies needed to achieve it.

In the absence of a coherent housing program formed by the Executive branch, I will offer my view of what the Federal housing goal should be as well as the strategies that would serve as the framework for meeting the housing goal In addition to the obvious social benefits, the by-product of this approach is a spur to general economic recovery through stimulation of the housing construction industry.

A healthy housing construction industry benefits everybody by creating jobs in its own sphere as well as in allied industries. It contributes significantly to the health of the economy and would help rescue our beleaguered saving and loan institutions from financial ruin. Stimulation of the housing industry has proved to be the lynchpin of economic recovery during past periods of recession.

National Housing Policy

Goal: To assure safe, suitable, affordable housing in viable communities with equal access for all.

I do not need to dwell on the gap between the goal and reality. However, I think it is useful to discuss

NEW YORK STATE
DIVISION OF
HOUSING AND
COMMUNITY
RENEWAL

briefly the major areas of need:

- o Lack of affordable housing.
- o Lack of adequate suitable supply.
- o Lack of equal access to housing.

1. Lack of affordable housing is a problem in cities and rural areas, particularly for those with low-to-moderate incomes.
   - o The average cost of a new home increased dramatically in the last decade -- in 1970 more than half the population could afford the median priced new home -- by 1979 less than 15%.
   - o 72% of all New York City families live in rental housing; of that group:
     - 31% pay more than 40% of income on rent.
     - 1 out of every 5 had income below the poverty level.
   - o Rural New York has a growing number of elderly on fixed-retirement income.
   - o In 1970 HUD estimated that over 300,000 low- and moderate-income households were paying burdensome rent-to-income ratios. Today the problem has worsened.
2. Lack of adequate supply of suitable housing is a problem in urban, suburban and rural areas;

and for special populations such as the elderly, disabled, single-parent families, the "homeless".

- In 1978 HUD estimated that 6 million families live in substandard housing and another 2 million families live in crowded housing units.
- In 1970 HUD estimated a need for 2 million new units each year to meet demand. In the last decade, the goal was met in 4 years only.
- In 1970 HUD estimated that 650,000 New York State households were substandard.
- In New York City alone 79,000 occupied rental units are classified as dilapidated.
- 2.7 million rural New Yorkers live in 15% of the State's housing stock; more than half built prior to 1939. Much of it is located in areas with inadequate water and sewer service.
- In New York City 71% of elderly pay more than 25% income for rent.
- Some estimates of the total number of "homeless" in New York State are as high as the total population of Santa Fe, New Mexico.

3. Lack of equal access to housing persists because of discrimination in the sale and rental of housing; minorities are discriminated against by

banks and other lending institutions and do not have equal opportunity to participate in programs and share resources.

- In 1978 HUD survey on discrimination patterns found that housing discrimination still persists.
- Numerous studies have documented discrimination in access to financial resources to purchase or improve housing.
- The declining population and increasing concentration of minorities, the poor and elderly in core cities leads to an absolute decline in available real resources.
- The high cost of housing raises additional barriers to minorities' access to suburban living.
- Suburban communities continue to resist the location of subsidized family housing projects in their neighborhoods, restricting access to subsidized housing. Only a limited number of blacks benefit from housing assistance programs in suburban communities.
- Redlining, continuing abandonment and disinvestment in low-income areas and other practices have a disproportionate effect on minorities.

NEW YORK STATE
DIVISION OF
HOUSING AND
COMMUNITY
RENEWAL

What follows is a comparison of the provisions in the Administration's plan and those in H.R. 5731 against the four basic strategies. By juxtaposing the strategies with the two proposals, one can evaluate more clearly which approach best meets our goal.

Four Strategies for Improvement

I believe the following four strategies are consistent and necessary to achieve the goal of our overall housing policy.

1. Provide financial assistance to those who cannot afford suitable housing.
2. Provide financial incentives for private sector to increase supply in order to provide for those who cannot secure adequate housing on a market economy.
3. Strengthen and revitalize neighborhoods and renew investment in communities; bolster housing in tandem with support services.
4. Establish programs to insure equal opportunity and accessibility for minorities.

The following is a comparison of the administration's plan and H.R. 5731 with the objectives under the four strategies:

NEW YORK STATE
DIVISION OF
**HOUSING AND
COMMUNITY
RENEWAL**

Comparative Analysis

STRATEGY	PRESIDENT'S PROPOSALS	H.R. 5731 GONZALEZ PROPOSALS
1. Provide financial assistance to keep housing affordable	No program for emergency mortgage relief for owners faced with temporary problems in paying mortgages	Proposes funding of $760M for 76,000 single family homeowners faced with difficulties in making mortgage payments
	Eliminates Housing Counseling Assistance	Proposes $4 million for Housing Counseling
	$1.1 billion for public housing operating subsidies	$1.6 billion in public housing operating subsidies
	61,000 units of Section 8 Existing cancelled -- converted to voucher program	Proposes an additional 30,000 units for Existing Section 8 housing

DHCR Recommendations:

- Favor Emergency Mortgage Relief program. Decisions on targeting of funds should be determined by States in cooperation with HUD.
- Favor continuation of Section 8 Existing Certificate program. There should be a State set-aside of these funds for non-entitlement communities.
- Urge improved coordination between HUD and HHS in the targeting of welfare rent subsidies.

STRATEGY	PRESIDENT'S PROPOSALS	H.R. 5731 GONZALEZ PROPOSALS
2. Provide financial incentives to increase supply (availability)	Eliminates multifamily housing production	Proposes $1.3 billion for new rental rehabilitation program. This could produce between 60,000 and 100,000 new units
	Eliminates GNMA Tandem program	Proposes $1.9 billion for GNMA Tandem
	Ceiling on Finance Adjustment Factor (FAF) at 12% construction must be commenced by June 1, 1982	Codifies the ability of HUD Secy. to increase Section 8 FMR's to reflect increased interest costs, and makes development costs up to 14% mandatory
	Eliminates Section 235 Homeownership Program	Retains Section 235 program for 15,000 units and activities program for families below 130% median income
	Eliminates Section 312 Rehabilitation	+$69 million for Section 312 loans
	10,000 units of Section 202 elderly & handicapped hsg.	15,000 units of Section 202 elderly & handicapped hsg.
	Eliminates funds for troubled projects	Proposes $4 million for troubled projects

DHCR Recommendations:

- Favor retention of Section 312 program with sliding interest rate, targeting of funds to support other neighborhood revitalization activities, and tighter administrative controls to decrease loan default rates.
- Favor continuation of Section 202 program with increased role for States in the selection and targeting of funds.

STRATEGY	PRESIDENT'S PROPOSALS	H.R. 5731 GONZALEZ PROPOSALS

- o Favor the use of flexible subsidy funds for both federally and non-federally insured projects

3. Revitalize neighborhoods & community renewal	Deregulates CDBG program: eliminates low and moderate income family language; eliminates standard auditing & record-keeping functions	No programmatic changes
	Eliminates Section 108 loan guarantees	Proposes $100M for Section 108

DHCR Recommendations

- o Favor the continuation of the CDBG program with specific funding authorization for small cities and rural areas.
- o Urge better coordination between HUD and FmHA so that rural areas can take complete advantage of funding programs.
- o Retain those regulations for the Community Development Block Grant program which enhance the targeting of funds like the Neighborhood Strategies Area Program (NSA) and the Housing Assistance Plan (HAP). Retain requirements of citizen participation for CDBG Program.

STRATEGY	PRESIDENT'S PROPOSALS	H.R. 5731 GONZALEZ PROPOSALS
4. Protect right of equal access and insure minority participation in programs	No effective enforcement mechanism in HUD's fair housing authority Eliminates special HUD office responsible for insuring minority participation in federally assisted production and supply programs. Consolidated with overall voluntary services unit.	

DHCR Recommendation:

Resurrect fair housing legislation (H.R. 5200) initiated by the House and defeated in the Senate in 1980.

Other Housing Issues

There are three other housing-related issues, not addressed by the Subcommittee's plan which, I believe, are important and necessary to identify; namely, the proposed cut-off of funds to any localities with rent regulation; the housing voucher program; and changing eligibility standards for residing in publicly-assisted housing.

Rent Regulation:

The President's Housing Commission has proposed to cut off any type of housing assistance to those municipalities that have rent regulation. I believe this is essentially a local issue and any Federal legislation is improper, unsound and inconsistent with current policy. Even though I believe that improvements can and should be made in administrating rent regulation, its elimination in New York would undoubtedly cause severe financial pain for most and could result in the unplanned and unstructured removal of over 3 million individuals from their apartments. All this for little social or economic benefit.

Last year this subcommittee defeated a similar proposal in this area. I urge you to hold fast should it resurface.

Housing Vouchers:

The housing voucher program is designed to replace rent subsidies. In New York City there is a vacancy rate of 2%. Where will people there find housing?

The Administration argues that private developers will, if allowed to operate in a totally free market, produce the necessary housing. Past history disputes that view. Even during times of a healthy economy, the private sector could not be lured into certain fragile markets such as housing for low- and middle-income families without substantial government subsidies. It is this segment of the population

NEW YORK STATE
DIVISION OF
HOUSING AND
COMMUNITY
RENEWAL

most in need of assistance through some form of rent subsidies. I am not optimistic about the private sector filling this needs without subsidies and tax incentives. Vouchers won't do it.

In addition, I offer the following five concerns for your consideration:

(1) The commitment of resources is well below what is needed. There are more than 5 million low-income renters across the nation who live in decent housing but pay a disproportionately high percentage of their income for shelter.

(2) Housing vouchers do not balance financial and physical housing needs. Two million low-income renters still live in physically inadequate housing.

(3) Housing vouchers are less flexible than the current major program of Section 8 rent assistance.

(4) The voucher plan, with its entitlement approach, conveniently ignores the magnitude of the need and thereby denies housing assistance to millions of people.

(5) Experiments with housing allowances have largely been in small towns, not in major cities where most of the low- and moderate-income households are located.

Public Housing Eligibility Requirements:

Another proposal from the Reagan Administration would allow food stamps to be counted as income for the purpose of determining eligibility to reside in publicly-assisted housing. The argument that food stamps reduce out-of-pocket expenses for an individual, while true, is disingenuous because it overlooks the fact that rents for all forms of housing are increasing.

The food stamp program, much like the housing assistance program for low-income families and other cost-of-living subsidies, was designed to help individuals less able to care for themselves because of age, infirmity, loss of work, inadequate skills, lack of equal opportunity and other conditions and factors that rendered them disadvantaged and needy. From the Administration's point of view, the merit of this approach is that it reduces, on paper, the number of "truly needy" individuals, giving a false sense of progress. My view of this proposal is that it is unfair, cruel and represents another attempt by the Administration to eliminate the small economic gains this segment of the population has achieved.

We in New York understand the need for fiscal restraint, as well as fiscal responsibility. We know that scarce resources must be balanced with prudence and compassion. New York was able to avoid financial disaster and redesign its fiscal plan in line with the financial realities. This was done equitably, without placing our most vulnerable residents in jeopardy. If we are to ensure our nation's economic health, then this Administration, like the New York State Administration, must move housing and community development issues up on its agenda.

New Federalism is not the answer. As Governor Hugh L. Carey noted in a recent article in the New York Times:

"In the first year of the President's proposed 'new federalism,' New York State and its local governments would have to absorb a loss of Federal revenues of more than a billion dollars.

"The President's proposals signal a headlong retreat from our historic commitment to equitable treatment of all Americans, whereever they live. . .

". . . What is crippling states and localities throughout the country is not the complexity of the Federal system. It is the combined effect of huge Federal budget cuts, a severe recession that results at least in part from national economic policy, and borrowing costs that are constantly being driven upward by the Federal deficit."

NEW YORK STATE
DIVISION OF
HOUSING AND
COMMUNITY
RENEWAL

The housing needs of our citizens will not disappear because we ignore them or stop funding them.

Rhetoric won't solve the housing problem -- only money can do that. The development of a long range housing policy requires the commitment and assurance of future funds. We cannot ask the private sector to enter into the partnership of long-term financial commitments when government shows no interest in making such a commitment on its part.

The Federal government has had a long history of acknowledging its responsibility in housing. I am very encouraged that this Subcommittee through H.R. 5731 is determined to maintain this nation's commitment.

Thank you.

Chairman **Gonzalez**. Thank you, Mr. Berman, for your very valuable presentation, because I think you have hit the central issue, which is reaffirmation of national policies and programs that the Congress itself has established for in some cases as long as 40 years.

New Federalism to me is really a mislabel. It is old, not even wine, but old potions, new labels, but it is what I would call the counterrevolution, and I am not talking about the social revolutions in the 20th century, I am talking about the original American Revolution. It is counter because it shows a basic ignorance of even such things as the central message of Madison's presentation on behalf of the Constitution in Federalist Paper Number 10, which essentially addresses this issue.

The President is telling us now that total dismantling of these programs is necessary, whereas the reason for the Revolution and for the Constitution was to obtain some kind of a central and overall power democratically rather than concentrate power in a few hands. I would call the President's approach counterrevolution.

But be that as it may, for the record, would you mind giving your assistant's title? You don't have a "U" in your name.

Ms. **Knepper**. No.

Chairman **Gonzalez**. You see, in Texas, in my area, that is a very historic name from some of the original German colonizers in the area, and we would say "Knupper." How do you pronounce it?

Ms. **Knepper**. It is Sydelle Knepper.

Chairman **Gonzalez**. You don't pronounce the "K" at all?

Ms. **Knepper**. No.

Mr. **Berman**. Assistant Commissioner for Development.

Chairman **Gonzalez**. Thank you very much.

I just have one question. If the Congress passed successfully this portion of the rental housing production program, as we outlined it in H.R. 5731, what type of subsidy mechanism would the State of New York likely use?

Mr. **Berman**. You will have to give me a little more of a hint. If you pass yours with rental assistance, I won't need it. Which one is this?

Chairman **Gonzalez**. Well, I mean, what form would the subsidy likely take, say, in the State of New York? What I am getting at is the desirability of or the importance of flexibility.

Mr. **Berman**. Go ahead, Sydelle.

Ms. **Knepper**. In regard to the $1.3 billion for the rental program, we would probably——

Chairman **Gonzalez**. This is the production program we are talking about.

Ms. **Knepper**. We would expect, we would encourage the use of community development block grants by localities. We have a housing development fund program which works similar to the old 106(b) program, which was a seed money, interest-free loan program that HUD ran, I don't believe they funded the program several years and we would encourage that program to be used with this new rental rehab program as well.

Mr. **Berman**. With our housing development fund which we have, which is similar to——

Chairman **Gonzalez**. Your State——

Mr. **Berman**. We have a State housing development fund. It allows us to basically put the front end cost out for self-cost, et cetera, and to do it until the permanent financing is done.

Chairman **Gonzalez**. Well, your stated recommendations are very valuable in that specific regard, and I appreciate it.

My time is up. I will ask unanimous consent that I may be permitted to submit, if necessary, and it may not be, after we have heard the others, but not more than two or three questions for the record in time to answer for the transcript.

Chairman **Gonzalez**. Mr. Stanton?

Mr. **Stanton**. Thank you very much, Mr. Chairman.

Mr. Berman, we thank you for your presence here.

I get the distinct impression, for some reason, that you are not necessarily crazy about the administration's housing programs.

Mr. **Berman**. If I thought it would solve the problem, it would not bother me.

Mr. **Stanton**. Just one question, one observation. Did the State of New York opt for the small cities program?

Mr. **Berman**. The first year, we did not opt for it. We are studying it now. It has been hard to make that decision on the small cities program for two or three reasons. No. 1 is that the regulations were sort of hanging out there, and No. 2 is that money becomes an issue. And No. 3 was the long-term commitments. There were already a lot of multiyear agreements that had been made by HUD for some of our small cities, and quite bluntly, it is possible that the amount of money that was going to come down was even less than the commitments, so there was not much to do.

So, it is those three areas that we are exploring. We now have it under consideration for the next round. But the problem with that is that it also does not earmark money for rural, and I think it is worthy to take a look at the rural areas. It is a slightly different problem, and slightly different uses than our small nonentitlement cities.

Mr. **Stanton**. Would that be more because of the farmers home program, within the farmers home jurisdiction, rather than the program itself?

Mr. **Berman**. From your vantage, it is a jurisdictional question. From our vantage, Farmers Home does not have for us a block grant program for the rural areas, and if you look at basics in terms of infrastructures and water and sewer lines and those sorts of things, some small commercial development, it becomes pretty important.

Mr. **Stanton**. One last question. Would you be in favor of additional funding for your State program where there is targeting of the additional funds for housing under the CDBG program?

Mr. **Berman**. Absolutely. I think that some of our cities have done well in terms of taking some of their block grants and using it for housing. I think that the nature of the housing prices demands now focused attention to it.

Mr. **Stanton**. Thank you, Mr. Chairman.

Chairman **Gonzalez**. Thank you.

Mr. Mitchell?

Mr. **Mitchell**. Mr. Berman, thank you very much, especially for your statements on pages 4 and 5, the reference to discrimination in housing. I commend you for them, but I would suggest, with all due sincerity, that I don't think we will see any kind of action supportive of the positions you want to take. The administration has made it very, very clear that it is opposed to any form of affirmative action. This has been articulated by the Attorney General. Some of the black spokespersons in the Reagan administration have railed against affirmative action, and frankly, you are not going to accomplish any diminishment of discrimination in housing without an affirmative action program.

I hope you will retain your commitment at the State level and pursue it vigorously. I say this not to denigrate any Republicans on this committee. I look at Bill Stanton, who I think is one of the finest and most decent human beings I know, who would oppose discrimination in any form, but to take a position——

Mr. CARMAN. I would hope you would include me in that, too.

Mr. MITCHELL. Well, I don't know you as well.

Mr. CARMAN. There is always hope.

Mr. MITCHELL. I have a couple of questions, so let me finish, because this 5 minutes goes very fast, but I do want to reemphasize the point that we will fail unless there is an affirmative action program along with law. A couple of quick questions.

What is being proposed by the administration? Its housing program, I think, is disastrous, but that is not enough. The felony is compounded by some administrative actions that are being taken at the present time. By way of illustration, it is my understanding that a sort of moratorium or freeze has been imposed by the administration on a number of priorly approved projects that developers have worked on for years. They have made the investments, and suddenly they find they are not going to be funded. Is this happening in your State?

Mr. BERMAN. Yes. The answer is yes.

Ms. KNEPPER. We have about 20 projects that are in our State set-aside pipeline which are in the process of development anywhere from conditional commitment prior to closing that cannot close at the present time because they are not financially feasible without additional section 8 contract authority or a lower interest rate.

Mr. MITCHELL. All right. I think that is happening all over the country.

Mr. BERMAN. Yes, sir.

Mr. MITCHELL. One more question in that area. In your opinion, would this type of administrative development discourage the private sector from seeking to enter into housing developments in the future?

Mr. BERMAN. There is no question that it does. It not only signals a retreat from an original position, but more basically and more fundamentally, it says, we are not interested in long-term commitments. You are not going to get people of financial means to invest their hard-earned dollars into future commodities if we are not prepared to make those future commitments. We do it in the defense industry every day and think nothing of it, and yes, we have a healthy economy in the defense industry, but we are willing to make long-term contracts, sometimes way long, and so it is prudent for a financial investor to invest in.

The worst thing here is the signal that said, now that we are changing, we are not interested in investing in housing in the future. You remember when we told you back when that we were committed and we put the money aside, we made the conditional approvals. Well, we are taking those back.

Mr. **Mitchell**. Full faith of the Federal Government.

Mr. **Berman**. I think it damages credibility.

Mr. **Mitchell**. I hope I have time for one more quick question, and that is with reference to the section 312 program, which had a salutory effect in my city of Baltimore. It has been administered well. You propose a sliding interest rate on section 312. In that proposition, would you suggest some kind of ceiling on that sliding interest rate, so that it does not exceed *x*?

Mr. **Berman**. There is not enough money in the program to take care of all people, so therefore you would want the income guidelines to have a limit, and then the percentage of affordable interest that they can pay has to have a limit.

Mr. **Mitchell**. What would be a reasonable top on a sliding interest rate?

Mr. **Berman**. You are now talking about 9 or 9½ percent, and I think that is the right range.

Mr. **Mitchell**. Thank you very much, Mr. Chairman.

Chairman **Gonzalez**. Thank you very much, Mr. Mitchell.

Mr. **Stanton**. Mr. Chairman, I wish to apologize to the panel. I got a call to come down to the Enterprise Zone announcement at the Rose Garden, so I will represent everyone here.

Mr. **Frank**. No, don't represent me. [General laughter.]

Mr. **Carman**. You are going to the Rose Garden for the Enterprise Zone?

Mr. **Frank**. That is going to be the first one.

Chairman **Gonzalez**. I never knew it had been removed from the disaster area category. [General laughter.]

Mr. **Carman**. The Rose Garden or the Enterprise Zone?

Chairman **Gonzalez**. Both. Well, we understand, Mr. Ranking Leader, and we appreciate your presence here.

Mr. **LaFalce**. Mr. Chairman, before Mr. Stanton leaves, I think that he should be aware of the fact that there is going to be a bill on the suspension calendar today mandating that he file for reelection by this Thursday, if he doesn't do so voluntarily on his own. It is my understanding that he has not filed for reelection. Is that right?

Mr. **Stanton**. That is true.

Mr. **Mitchell**. I second that, if you put that in the form of a motion. [General laughter.]

Chairman **Gonzalez**. Mr. Carman?

Mr. **Carman**. I apologize to the members of the panel for not having an opportunity to be here earlier. I would like to——

Chairman **Gonzalez**. Well, you are from New York, aren't you?

Mr. **Carman**. Now I remember. I would like to ask you about what you think of the efficacy of the 235 program per se. Are you in favor of that continuing on or not?

Mr. **Berman**. Again, the 235 program as it is now structured is a worthy program. There is no question that you do need some help for single family homes, et cetera. I would particularly favor some more of what I would call targeting by the State in terms of the priority areas in which to inflow the money, but I think the program is desirable and the program ought to be maintained.

Mr. **Carman**. One of the reasons I raise it with you is that I recently became aware of a situation where a couple had $30,000 in the bank, and a salary between them of $25,000 a year plus, and they were still able to qualify for the program and purchase a $60,000 home. It just seems to me that in that kind of situation, we are not reaching with our Federal dollars the people that need to be reached.

So, while we can talk about 235 having a valuable overall tone to it, it seems to me the people who should be reached are not being reached. Would you tend to agree with that, Mr. Berman?

Mr. **Berman**. I think that I would have to say there are some people who are being reached who fall in your definition of should be reached, and there are those who do not. So I wouldn't want to say that I don't think 235 is reaching the right segment. I think that there can be some tightening and some more targeting of it so that it can have a higher——

Mr. **Carman**. Having supervised the closing of about 1,000 of them, I can tell you that from my own experience that I have seen too many people targeted in the category I have just described here. I would just like to raise one other question with you pertaining to section 8 housing in general. I know the city of New York has had a great concern about continuing it. I am very interested in the construction work that is associated with it, but I am inclined to think that we probably do not reach as many people as we ought to be reaching with the amount of money that is being expended for section 8 housing.

In fact, by the time we are done with all the other costs, each apartment probably costs several hundred thousand dollars. One figure recently given to me by a very senior administrator in the Housing and Urban Development Authority was $500,000 per unit. Certainly a substantial amount of money is involved. We have $5 million for rent. I have always felt that if I spent that kind of money, I wanted to own the place.

The other part is, we have an authorization for $39 million for the rents. We don't want to lose our commitment to public housing for senior citizens and low-cost family housing, which is certainly needed throughout the Nation, but it seems to me that section 8 housing is not accomplishing that, keeping in mind that it had its genesis in the Republican administration a couple of years ago.

Would you care to comment with regard to that, aside from the Republican part?

Mr. **Berman**. I have tried in the text, and when I answered your colleague, Congressman Stanton, I don't really care who proposes it and where it came from. If it works, it works. If it doesn't work, it doesn't work. Section 8, again, if you look at some of our upstate developments, section 8 turns out to be as cheap or cheaper to build in New York State as any State in the Union. And when you look at the level of rents in rent subsidies, you will find that it is within any target you want. The problem is if you build subsidized housing in New York City, Chicago, Detroit, Buffalo, et cetera, housing costs more, whether you do it section 8, subsidize it section

8, whether you subsidize it off of an interest writeoff, whether you subsidize it—no matter how you subsidize it.

Mr. **Carman**. I am very much aware of this, Mr. Berman, having supervised many of them. My question is: Do you think there is a place in here for some sort of a turnkey approach, the old turnkey approach, with certain modifications that might have a salutory effect on the overall process?

Mr. **Berman**. I remember the turnkey. We just did some of those, and the city is doing more.

Mr. **Carman**. It is pretty much being phased out at this point, and the question is whether or not we should be examining that with some other modifications that would make it more effective.

Mr. **Berman**. I think there is no question that we ought to take another look at both the turnkey and the section 8 program and see how we can do it more cost effectively. I am not sure the fair market rent does that.

Mr. **Carman**. I would tend to agree with you. I didn't have a chance to read your entire statement, but I would gather that you don't think the voucher system is the be all and end all to the entire housing problem.

Mr. **Berman**. I think it is counterproductive.

Mr. **Carman**. Is there any place for us to use a voucher system at all in conjunction with other kinds of public housing? Do you think we should have any of it at all?

Mr. **Berman**. Well, you have a small type of voucher program with the existing section 8, and perhaps where you have an oversupply of housing that is adequate. You field tested it in a couple of small communities with some marginal successes. I am not opposed to trying it, again, but we know it doesn't work if there is inadequate supply. We know it doesn't work. We have a whole list of conditions. I am sure there are parts of the country where the conditions are receptive, and we ought to try it. We should not think that we have to find one thing that is going to solve everyone's problems.

Mr. **Carman**. Thank you, Mr. Chairman.

Thank you, Mr. Berman.

Chairman **Gonzalez**. Thank you.

Mr. LaFalce?

Mr. **LaFalce**. Thank you, Mr. Chairman.

Just a specific question and then a very broad question. Specifically, do you have any data regarding the number of households that might be in need of emergency-mortgage-relief assistance because of the distressed times we find ourselves in?

Mr. **Berman**. The answer is, I don't have that data. I understand the issue. I think it is a real issue, but——

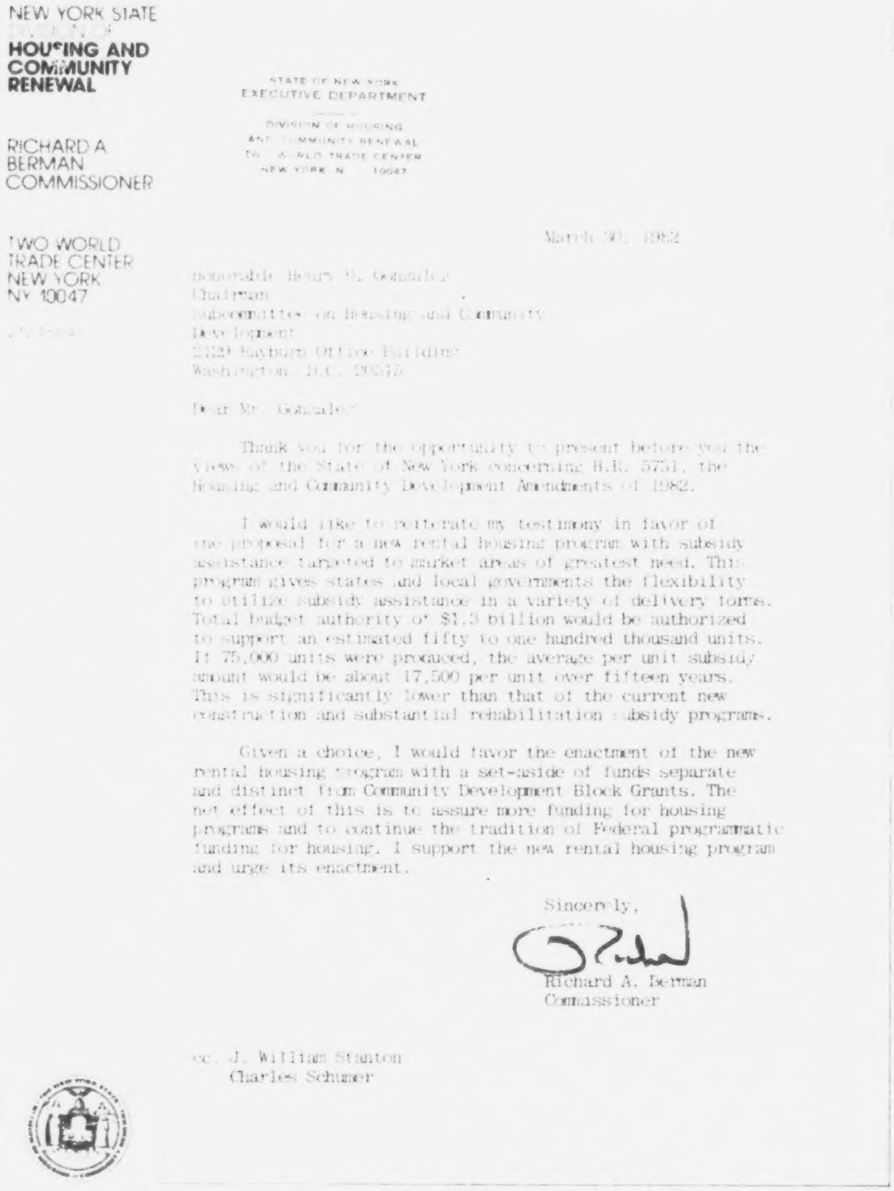
Mr. **LaFalce**. Who would have that? Mickey Siebert?

Mr. **Berman** [continuing]. Only to the extent that the banks would report that to Mickey, and I don't think they do, to be honest with you.

Mr. **LaFalce**. You called for an emergency mortgage relief program, and I am just curious if we can in some way document the need.

Mr. **Berman**. I think we will take as a task, Congressman, to go back and see if we can give you all some documentation that will help you support the need.

[In regard to the above colloquy, Mr. Berman sent the following letter, dated March 30, 1982, to Chairman Gonzalez:]



NEW YORK STATE
DIVISION OF
HOUSING AND COMMUNITY RENEWAL

RICHARD A
BERMAN
COMMISSIONER

TWO WORLD
TRADE CENTER
NEW YORK
NY 10047

STATE OF NEW YORK
EXECUTIVE DEPARTMENT
DIVISION OF HOUSING
AND COMMUNITY RENEWAL
TWO WORLD TRADE CENTER
NEW YORK, N.Y. 10047

March 30, 1982

Honorable Henry B. Gonzalez
Chairman
Subcommittee on Housing and Community
Development
2129 Rayburn Office Building
Washington, D.C. 20515

Dear Mr. Gonzalez:

Thank you for the opportunity to present before you the views of the State of New York concerning H.R. 5731, the Housing and Community Development Amendments of 1982.

I would like to reiterate my testimony in favor of the proposal for a new rental housing program with subsidy assistance targeted to market areas of greatest need. This program gives states and local governments the flexibility to utilize subsidy assistance in a variety of delivery forms. Total budget authority of $1.3 billion would be authorized to support an estimated fifty to one hundred thousand units. If 75,000 units were produced, the average per unit subsidy amount would be about 17,500 per unit over fifteen years. This is significantly lower than that of the current new construction and substantial rehabilitation subsidy programs.

Given a choice, I would favor the enactment of the new rental housing program with a set-aside of funds separate and distinct from Community Development Block Grants. The net effect of this is to assure more funding for housing programs and to continue the tradition of Federal programmatic funding for housing. I support the new rental housing program and urge its enactment.

Sincerely,

Richard A. Berman
Commissioner

cc. J. William Stanton
Charles Schumer

Mr. **LaFalce**. I am fearful with the tremendously high unemployment right now, and I don't know whether it is going to abate, that we might be facing a problem now similar to the problem we had in 1975 when we did come up with the special emergency mortgage relief program. This would vary from State to State and region to region within the State. In my Erie-Niagara region we have a composite reported unemployment of 12.5. I think the real unemployment rate is closer to 20 percent.

Mr. **Carman**. Could I interject for just a moment? If we were to do something like this, I would commend to you the Soldiers and Sailors Civil Relief Act of 1940, I think it is, which would be worth taking a look at. It might have some effect if we have it at the Federal level pertaining to military personnel. It might be the type of legislation that could be useful. It is setting up a mechanism.

Mr. **LaFalce**. If you have any suggestions of your own for ways to implement such a program, I would be very interested in that. I think we are experiencing a lot of difficulty in western New York along those lines, and the financial institutions are in a situation where there is not much they can do about it. I think they will exert tremendous forebearance. They don't want to become holders of real estate.

Mr. **Berman**. Right in our own area, remember, we had a bank that over a weekend began to call in some of those mortgages, and we all got involved, and you were a key player in stabilizing that situation.

Mr. **LaFalce**. We got them to reverse the situation rather quickly, like 9 o'clock Monday morning.

Mr. **Berman**. And I thank you for that. We could not have done it without your help, and there are a lot of people who were very uncomforable that weekend, but we will try to—we owe you those specifics. I don't have them here.

Mr. **LaFalce**. Dick, a general question now. Would you briefly describe to me the functions, duties, responsibilities, and activities of the division of housing in New York State? New York State has been criticized in the past for having a very, very fragmented approach to housing, with no central office to establish a housing policy, a housing delivery system, housing in the largest sense.

Would you care to describe what you inherited, and what you have now?

Mr. **Berman**. OK. Let me try to do it fairly briefly, and then we can pick it up again at lunch. We have what we call a public portfolio——

Mr. **LaFalce**. It has bearing, too, on the question of whether or not the Federal Government should be delegating tremendous responsibilities to the States. I think, in large part, a great many of the States do not have the delivery system capacity to handle these Federal programs. I for one seriously questioned whether New York State had the existing capacity to take over the small cities program, for example. I did not think that you did, and I do not think that you do now.

Mr. **Berman**. We are prepared to make a case. It has been a checkered history in New York State in housing, from being out in the lead with Mitchell-Lama and back and forth.

Roughly, we have responsibility in four areas. One is the public portfolio. We supervise a public portfolio which includes the HFA financed, UDC financed, and some earlier projects which were the State comptroller's job, which predated. Those projects have about 115,000 units, a little more than 115,000 units, about 600,000 New Yorkers living in them, and we are the supervising agent in that we approve their budgets, we set the rent levels, we approve all contracts for repairs and management, et cetera. Those are statewide.

The second major area is the State building code and the fire code. We have the building code and the State fire code which have been adopted in a majority of our communities and we have a charge by 1984 to propose a uniform method for our State fire and building code.

Mr. **Mitchell**. Excuse me, Mr. Chairman, I am having a little difficulty hearing the witness, and I am especially interested.

Mr. **Berman**. Sir, we have the responsibility for a statewide building code and fire code, in which we work with a lot of the municipalities which do not have the resources at hand, to review proposals and to get a sense of what is happening.

We have a third major area that—the third major area is community renewal program. In the community renewal program there are four or five major programs which we operate. We have a program which now has about 150 neighborhood preservation groups which are not-for-profit, community-based organizations throughout the State which we fund annually at about $10 million.

And they have been able over the last 5 years to put in place local structures concerned with housing, working on housing. The issues range from tenant organizations and tenant relations to major leveraging of Federal and private bank dollars, some insurance companies, and some major industries.

Their efforts have resulted in over 100,000 new or substantially rehabbed units. They have been able to leverage our moneys 5 to 1 with outside money and have been a great source.

Last year, we started a companion program for rural preservation programs, of which we have started some rural groups, about 50, and a several-million-dollar expenditure.

We have been working in terms of the 107 program and technical assistance to small cities, and working with communities primarily through our Buffalo and Rochester offices.

We have administered the heat and rent subsidy programs and our own capital grant which is another type of operating subsidy of 100-percent State money for 2,300 families.

The fourth is our development area, which Sydelle heads, which has the responsibility for our administration of section 8. We are responsible for sending out the NOFA, the selection review of bidders, and organizing priorities. Our HFA is then the financer, in most cases, although some may choose to do it independently.

The other major effort that we have undertaken is to try to, again, not throw stones unless your house has at least one brick window in it, and that is, we have been trying to focus housing policy in the State, and to articulate that and to coordinate it. And in the Governor's state of the State message, this year he clearly identified the division as that point in State government.

I sit on the Board of the Housing Finance Agency, I sit on the Board of the Sonyma, I sit on the Board of the Mortgage Loan Corp. and in that way we try to coordinate our State efforts. We are in the process of finding that in trying to set and implement policy, there is a dearth of data upon which to build an adequate housing policy.

We have just led a request for proposal in the neighborhood of $100,000 with the precise effort and objective of providing that data base so that we can articulate where the need is, what is the need, how is it different in rural, suburban, and urban areas so that we can better allocate and manage our own efforts.

Mr. **LaFalce**. We will have to pursue this later. I want to apologize. I am chairing hearings of the Small Business Subcommittee at 10:30, 5 minutes ago, which I have to go to.

Mr. **Berman**. Thank you, very much for coming.

Chairman **Gonzalez**. Before the gentleman from New York leaves, I do want to interject this. The best figures that I have been able to obtain as of last month, would reveal that New York, on an average, in a period of about 45 days preceding February, had an increment increase of a little better than 33 percent in foreclosures, the foreclosure rate, not moratorium on payments, but foreclosure.

And interestingly enough it parallels areas in California where you have high rates of unemployment, as much as 12 percent, in semirural areas. But still California is such a State that when you say semirural, you really are not differentiating too much.

Mr. **LaFalce**. If I could interject, it is probably extremely significant because banks are much more reluctant to foreclose today than they were in 1975. When they did foreclose in 1975 they found out that they had a lot more difficulty after foreclosure with vacant housing than they would have if they had individuals living in that housing, and even not paying rent.

So I just think that might mean it is an alarming situation.

Chairman **Gonzalez**. It is, and that is the reason for our title VI.

Mr. **Berman**. Absolutely.

Chairman **Gonzalez**. Mr. Vento.

Mr. **Vento**. Thank you, Mr. Chairman. I appreciate the witnesses, all of the witnesses that are here today, although I do not have time to spend this morning but in looking over the statements, I commend the chairman for bringing these witnesses and making the committee record that he is making.

I think that there are some basic questions. Obviously, the administration offers no real housing program. We always have trouble with those who need assisted housing but today the definition of assisted or the need for assistance is almost universal with just the exception of the highest income individual going into the market at 17 percent.

So the question really, and I think all of us have to come to grips with this, is looking at the whole panoply of housing-assistance programs today, is that they really end up helping those who have moderate or higher income. You still cannot, unless you come in with very deep subsidy, a tandem program so to speak, end up getting down to the lower income levels. That is one of the things, that is the problem with cutting off the pipeline of assisted housing is that those programs that we know during bad times help these folks get housing.

So I think that the question that we have to look at now is, during these times, should we really get in, we cannot buy back the difference in terms of interest rates that exist. The fact is that the question of getting into that in terms of assisting others, is what we are looking at today, in hopes of trying to provide some economic stimulus, in hopes of trying to maintain the institutions and framework of housing and people that exist, whether it is the Housing Finance Agency, whether it is your organization, whether it is carpenters, or builders, or so forth and so on.

So we really have been doing a lot of damage control here. We are talking about reshuffling the dollars around that we have, rather than really addressing these same needs. We are changing the focus of the needs and what we are able to do and I wonder if that concerns the folks and what we ought to be careful as we are in the process of doing that so that we do not end up, hopefully, after we climb out of this recession, with really a program that is a mile wide and an inch deep and does not help anyone.

What do we have to be careful about here, Mr. Berman?

Mr. **Berman**. I guess that is why I would suggest that, and I think that some of the questions that were raised earlier about targeting, not only geographical targeting, but who do you want the programs to really help.

I would argue that we have the greatest responsibility to those who are normally left out. Those who are the most vulnerable, those who are disenfranchised from the current system. And therefore, even though the easier route out, the way you can spend more of your money, if you will, is to help those who would be helped if you were just able to reduce the cost, whether it is interest rates, or front end, or whatever, by 1 percent, those are the groups, in all candor, that will be the first out when the economy becomes healthy again. So, therefore, I guess that I would urge you to concentrate and focus on where the problem is the most severe The liklihood is that any change in the economy is not going to assist the lowest income—that is the aged, that is the disabled, that is the minorities, that is some of the rural, and Indians, and minorities. That is where our basic responsibility and commitment is.

Yes; we have concern about the middle class. Yes; we have concern about the first-time home buyer, but it seems to me that I think that you do have some concerns, as we all do, about putting a little money out there for all of the categories. I think that you have to target it, and I think that it is an important national issue.

Mr. **Vento**. Thank you, thank you, Mr. Chairman.

Chairman **Gonzalez**. Thank you, very much, Mr. Vento. Mr. Frank?

Mr. **Frank**. Thank you. I want to talk to you on one issue that we dealt with last year, when we were doing the authorization. Obviously, we all want to win, not all, because the administration is not part of the consensus, but many of us want to get construction back going again. One of the other problems, obviously, is the maintenance of the existing stock, particularly various levels of subsidies.

A lot of attention has been given to the inadequate willingness of the administration to keep public housing going. One of the things that became an issue last year was an administration proposal to give them greater ability to take 236(d)(3), other assisted, moderate housing, and get rid of it in a way that would remove any income limitations or any rent limitations.

Basically, they asked us for an ability, when those projects went into default, to be able to sell them with no restrictions. In some cases, I think, that we would lose them from subsidized housing stock.

I am just wondering if you had any experience with this last year with them under that, and what your general sense is about that. Because it seems to me that if we do not simultaneously do a better job of protecting existing subsidized stock, we are going to exacerbate the problem of an inadequate construction level.

Mr. **Berman**. We have not particularly had any experience with it, because most of that housing stock returns to the municipality. It is now HUD's responsibility. I think that you cannot have it both ways. You cannot put enough money in it to keep it going as a subsidized housing.

If you fail from the Federal Government to put enough money in it to maintain it and keep it so that you can provide substantial housing for the poor, middle income, low income, whatever the category was, once you fail to do that, if you are always going to fail to do that, then you have no real option but to let it go to another group of people.

I think the policy issue is the fundamental one. We do have responsibility to those people and it would be a much better investment to invest in that existing housing stock and make sure that it stayed in good shape. We provide subsidies so that it can stay on the market for moderate- and low-income people. That is superior to withdrawing the subsidy, and giving it to another group of people, and then still have the same problem, which is where are you going to house the low- and moderate-income people.

Mr. **Frank**. So per unit cost, the cheapest thing that you can do is to make sure that you keep whatever stock you now have for various levels of recipients functional for them.

Mr. **Berman**. Right, even though it is inadequate, it is clear that you do not want to lose that while you are chasing something else.

Mr. **Frank**. The point we have to keep in mind is when we are talking about construction levels for new housing, given the policy that HUD wanted last year, and given and other trends, we may well be losing more subsidized units than we are constructing. And that obviously, is a problem.

Mr. **Berman**. Absolutely.

Mr. **Frank**. I will yield the balance.

Chairman **Gonzalez**. Thank you, very much. Mr. Evans?

Mr. **Evans**. I pass, Mr. Chairman.

Chairman **Gonzalez**. Thank you. Before you get going, Mr. Schumer, I think that it is my responsibility to say that he is a fellow New Yorker, and I guess that he had just come in from New York, I do not know. Otherwise, he would have been here first.

Mr. **Schumer**. That is correct, Mr. Chairman.

Chairman **Gonzalez**. But he has been very impressive to me, very inspiring, because even though he is young, he is not inexperienced because he served in the State legislature, and he has come in here running, as Speaker McCormick told me when I got here.

Mr. **Schumer**. Both ways. [Laughter.]

Chairman **Gonzalez**. In the meanwhile, I have been aware of one of those things that happens. We have a saying in Spanish coming back from the old ranch days, "Caballo viejo mata potrero," meaning that "an old horse will kill a young horse." You know, if they ever get in and the young horse defies in the corrals, and in Mr. Schumer's case, I notice where the New York papers had a big picture and a big spread about how his colleague from New York, Solarz, had saved rent control.

Well, the truth is that Schumer is the one who did it. Mr. Solarz came in during the conference for about 5 minutes, and I will give him credit. But I do not think that it is fair to let this experienced Congressman, Representative Solarz, come in and probably take the credit that properly belongs to Mr. Schumer.

You also referred, and I thanked you before for your support for the main thrust, if not the entire bill we are presenting, but Mr. Schumer had a hand in forging this bill.

And I think that in all fairness the record should show it. Now, Mr. Schumer you are recognized.

Mr. **Schumer**. Thank you, Mr. Chairman.

As a "young horse," I want to thank you for those kind words. I am happy to work together with anybody in the delegation for the things that we believe in.

There are a couple of questions that I had. I was a little bit concerned about a couple of your views on the rental production program, and maybe Mr. Stanton, in particular, when he was here, did not really understand what you were saying. And I would like to go over those comments.

When we put together this bill under Chairman Gonzalez' leadership, we felt that it was extremely important to have a housing program, not just a block grant or a community development program, in which the push and pull of politics, particulary in New York State where we have a great shortage of money, would preclude us from running a genuine housing program.

The administration has its voucher program, which many of us dislike, because it is not a housing program.

Our worry is that if we put the same amount of money, or tried to put the same amount of money, that we are putting into housing programs, the community development funds will go for other things and not create new housing.

Now, I would just like your views on that. I would like to reask the question that was stated before.

Would New York State actually favor, instead of a $3 billion housing program, adding that money into CDBG?

Mr. **Berman**. No; how specifically I thought I answered, and if I did not, let me respond specifically here: I favor a separate block grant for housing.

You have talked about a UDAG for housing, and so forth—and I was clear—I am saying that you have to isolate the housing money. We also are very excited and support your $1.3 billion rental rehab, as I would describe it and you probably have a fancier name for it, and said that we in New York State were prepared not only to support that, but we thought our housing development fund, which allows for some seed money and for some front-end funding, would make that really operational.

Even though HUD had the authority under its 106(b) provisions which had not been funded, we were prepared to move ahead on that in New York State.

Mr. SCHUMER. Let me ask you this. If you had a choice of the program we proposed, or adding the same amount of dollars into CDBG, which would you prefer? I might state that this would not be likely to happen, because if this committee proposes to just add money to CDBG, it is going to be cut, but assume that we could reserve it.

Mr. BERMAN. This program.

Mr. SCHUMER. I think that it would be helpful if you would just send that in a letter to me or more appropriately to the chairman with a copy to Mr. Stanton. Because I believe that he walked away with the impression that just adding money into CDBG was OK with the New York State housing commissioner. And I know that it was not your intention to give him that impression. So, I hope that you will clarify that.

Mr. BERMAN. We will clarify that.

Mr. SCHUMER. Good. Just another question. Last year, as you know, HUD ordered our public housing authorities to get energy emergency assistance funds from the State government. The New York City Housing Authority, for instance, got $12 million. This year we do not call it HUD any more, we call it HUD-OMB, because OMB seems to be making all the decisions. But HUD-OMB is proposing very unrealistic funding levels on the grounds that the States and localities can make up the difference.

We asked Commissioner Gleidman if the city could make up the difference in New York City. He said: "By no means." What is your view in terms of that?

Mr. BERMAN. There is absolutely no question that the State cannot pick up the shortfall from the Federal Government retreat, period.

Mr. SCHUMER. Do you think that you could pick up a little of it?

Mr. BERMAN. I would say, in this area, no.

Mr. SCHUMER. I think that too, is important, because the administration keeps telling us that we can do everything with CDBG money. My colleague, Mr. Frank, from Massachusetts, calls it the CDBG breeder reactor program. [Laughter.]

They cut the money, but they tell us that you can get more and more money out of it and it can go to housing and streets and this and that.

Mr. BERMAN. And that is it precisely. When I was asked the question earlier, had we not opted or had we opted into the Small Cities, we have not opted in because we are not convinced yet that it needs more money. We are convinced that it gives more flexibility but we are not convinced that there is a long-term commitment to fund the States to do it.

Mr. SCHUMER. OK. That settles things for me. I would like to say, Mr. Chairman, that Commissioner Berman has, and I am sure that my colleagues from New York, who made the 8 o'clock shuttle instead of missing it by 5 minutes, have told you, he has an outstanding record of service to New York State. He has performed miracles.

New York State has a fairly balanced budget, and one of the reasons was that we were one of the first States to humanely control our medicaid and other health expenditures, and that was really due to Commissioner Berman and his work as New York State's Health Commissioner. And if he can do half as well with housing, New York State housing would be in a lot better shape.

Mr. **Berman**. Thank you and thank you for your support. I want to again, reiterate, Mr. Chairman, that we have watched Chuck and we know others come in and take the limelight, whether it is in Wabash or somewhere else, and we are proud to be a part with and work with Chuck and his staff.

Chairman **Gonzalez**. Thank you, very much, Mr. Berman. We deeply appreciate the time you have donated and your presence. And your presentation was exceedingly helpful and very well done. And we are very grateful to you and we will continue an association and communication with you.

And thank you, Ms. Knepper.

Mr. **Berman**. Thank you, again, Mr. Chairman. And again we want to continue to be supportive of you because you have taken what could be a dismal area and kept the light of hope lit. So thank you.

Mr. **Frank**. Mr. Chairman, I would like to thank Mr. Berman and the other New Yorkers for letting me come to their hearing today. [Laughter.]

Chairman **Gonzalez**. Well, we will recognize the next panel and apologize to them. We were shifted to this room at the last minute, and therefore, it limited our ability to present more than three witnesses at one time.

So, now we can have three and we are going to recognize Dr. Henry B. Schechter, director of the Office of Housing and Monetary Policy of the American Federation of Labor and Congress of Industrial Organizations.

We have Mr. Leon N. Weiner, president of the National Housing Conference; and Mr. Richard K. Helmbrecht, president of the Council of State Housing Finance Agencies.

Mr. Evans, of course, being from Delaware and Mr. Weiner being from Delaware, I was going to say that unless one of the witnesses has a time problem, that we intended to recognize Mr. Schechter first and then proceed clockwise. But since we have Mr. Evans, we will give him the opportunity to introduce Mr. Weiner. He is your constituent, obviously.

Mr. **Evans**. Not only is he a constituent of mine, Mr. Chairman, but he has also been a friend for a long, long time. He happens to be a Democrat and I happen to be a Republican, but we are very friendly on many issues. We see eye-to-eye on some issues. Generally speaking, we are concerned about the housing industry. We are concerned about the economy. We believe that it can come back, and I think that we have a responsibility here in Congress to assist in a way that is equitable. I think the economic recovery program is fundamentally sound, but it is only going to work if everyone feels that they are pulling their weight and not someone else's. And we should not ask any segment of our community to bear an inordinate responsibility in the fight against inflation and high interest rates and unemployment.

The housing industry has led us into recession and historically it has led us out of the recession, and I think we have a responsibility to help. I hope we can help in a way that will not aggravate an already-bloated deficit, and help in a way that is fair. And I have some questions later on, Mr. Chairman, for each of the witnesses, but I appreciate very much your yielding to me.

And I might also say that Mr. Weiner is not only president of the National Housing Conference, but he is past president of the National Association of Home Builders. He is a very well-respected builder in our area, not only in the State of Delaware but throughout our region and throughout the country.

Chairman GONZALEZ. Thank you very much, Congressman; we deeply appreciate that.

Without any further ado, we recognize the preeminent Dr. Schechter, who has on many occasions helped us and appeared here, and we thank you once again.

STATEMENT OF HENRY B. SCHECHTER, DIRECTOR, OFFICE OF HOUSING AND MONETARY POLICY, AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS

Mr. SCHECHTER. Thank you, Mr. Chairman and members of the committee. I appreciate the opportunity to present before you the views of the AFL-CIO on H.R. 5731 and H.R. 5568. The AFL-CIO has been calling for actions to move the country out of the home building and financing crisis which is aggravating the national housing shortage, increasing unemployment and prolonging the recession. Chairman Gonzalez and Chairman St Germain are to be commended for introducing these two bills which move in the right direction.

In H.R. 5731, continuation of loan guarantees for localities and of the section 312 rehabilitation loan program, instead of allowing those programs to be phased out, will help to preserve urban neighborhoods and the older housing stock.

Title II of the bill provides necessary support for ongoing assisted housing programs and for programs that would help preserve the stock of assisted low-income housing. Thus, authority would be provided to support new construction units under the public housing and Indian housing programs, and additional units for the elderly and handicapped under section 202. These programs serve the neediest low-income families and should be continued.

The provision of adequate operating subisidies and modernization authority for the public housing program represents a prudent policy. The old public housing projects whose capital bonds have been amortized, provide low-income housing at a comparatively low annual per unit subsidy cost. This is a tremendous public investment.

Title II would also provide authority to support about 35,000 additional section 8 existing housing units. In order to avoid inflationary pressure, such authority should be made available only in markets where there is an adequate supply of the size of units needed by families eligible to receive existing section 8 housing assistance in that community.

The main new thrust for assisted housing production comes in a two-part program. Part A would permit activation of a section 235(q) program under which families with incomes up to 130 percent of local median income would be eligible. In 1980, based on the national average, about a $27,000 income would have been eligible. Payments by buyers could be as low as on a mortgage loan with an effective interest rate of 9½ percent. There would be $3.5 billion in budget authority to support the financing of an estimated 100,000 homeownership units with an average subsidy of $35,000 over a 10-year period.

Part B would be a new rental housing program with subsidy assistance targeted to market areas of greatest need. A given amount of subsidy could be used flexibly by the State or local governments in a variety of delivery forms. Total budget authority of $1.5 billion would be authorized to support an estimated 50,000 to 100,000 units. If 75,000 units were produced, the average per unit subsidy amount would be about $17,500 over 15 years.

Twenty percent of the units, an estimated 15,000, would have to be reserved for families with incomes not above 80 percent below the local median. In 1980, the national average level of that income would have been $17,000.

Part A and Part B together would provide an estimated 175,000 units, of which 15,000 would be for those with incomes below 80 percent of median and 160,000 for people with higher incomes. Equity requires—and the AFL-CIO urges—that budget authority to support Part B for rental housing should be increased substantially and made available for the lower income component.

Another area in which H.R. 5731 would halt the movement toward zero program levels is in rural housing. New construction units would be added under the low-income homeownership assistance program and also units under the rural rental housing program. The program levels deserve approval. There should be disapproval, however, of the section 402 provision that would increase the percentage of income that must be paid as rent by a tenant in an assisted unit from 25 to 30 percent.

The proposed emergency mortgage relief program in title VII would help many unemployed homeowners avert the loss of their homes. For reasons indicated, the danger of widespread foreclosures is imminent. This is a reasonable program which, in all likelihood, would result in little or no cost to the Government, and would provide stability to a real estate market which otherwise could have a far-reaching collapse in values.

One of the eligibility requirements of the mortgage relief program, however, is that mortgage payments must be at least 90 days delinquent. This should be changed to 30 days or 60 days, since there are a number of States in which mortgage foreclosure proceedings may be instituted when mortgage payments are delinquent for less than 90 days.

Enactment of the Home Mortgage Capital Stability Act, H.R. 5568, also would be prudent in the national interest. It would provide assurance against a wholesale collapse of thrift institutions by providing them with guarantees of reserves equal to as much as 2 percent of assets. This would prevent a loss of confidence in the depository institutions and allow them to restructure their portfolios toward a more sustainable basis.

One of the requirements for an institution that receives guarantees under the program is that not less than 50 percent of its annual net new deposits shall be used to issue mortgages. However, net new deposits would be defined "as determined by subtracting from deposits each year the total amount of withdrawals and of interest and dividends credited each year."

In tables published regularly by the Federal Home Loan Bank Board, new deposits received minus new deposits withdrawn is shown as net new deposits received, and the latter figure plus interest credited is shown as net deposit gain. That accepted, appropriate concept should be used in determining the amount of funds that would become available as investment stated as follows: "New deposits received plus amount of interest and dividends credited each year, minus the total amounts of withdrawals." That would assure a more meaningful flow of funds into residential mortgages. Under the proposed definition in the bill, the assisted institutions could end up with no need to invest in mortgages, even in a year with a substantial positive net inflow of deposits.

Also, to fulfill the objective of aiding homebuilding, the option for assisted institutions to meet one-half of their required mortgage investments through the purchase of mortgage-backed securities should be amended to provide that the mortgages collateralizing the securities, as well as the securities themselves, should have been originated after the effective date of the act.

With the recommended changes, H.R. 5568 would be an effective statute to sustain the viability of many troubled savings and loan associations for a period, and support some revival of homebuilding insofar as mortgage money currently would be made available for loans at about 12 percent interest rates. However, even at those interest rates, a high proportion of middle-income families could not afford to purchase homes. There is also a likelihood of a return to higher interest rates in the event of an incipient economic recovery.

There is no apparent willingness by the administration or the Federal Reserve to cease sole reliance on the tight money, high interest rate policy as an anti-inflation weapon, even though it has repeatedly led to more inflation, depression in homebuilding, and economic recession. H.R. 5568 does not address itself to the broader problem of a credit policy to reduce interest rates, a necessity for adequate housing production and economic growth.

The need for controlled credit availability without economically crippling interest rates can be addressed under the Credit Control Act of 1969, which presently is scheduled to expire at the end of June 1982. Since both the long-term viability of the thrift institutions and the ability of the housing industry to meet national housing needs, can be affected by exercise of the authority in the Credit Control Act of 1969, and it is in the jurisdiction of your committee; I urge you to make permanent or extend that act.

Thank you. That is my summary. I hope the entire statement will be in the record.

[Mr. Schechter's prepared statement, on behalf of the American Federation of Labor and Congress of Industrial Organizations, follows:]

Testimony of Henry B. Schechter

Director, Office of Housing and Monetary Policy

American Federation of Labor and Congress of Industrial Organizations

on the Housing and Community Development Amendments of 1982 (H.R. 5731)

and the Home Mortgage Capital Stability Act (H.R. 5568)

Before the Subcommittee on Housing and Community Development of the

U.S. House of Representatives Committee on Banking, Finance, and Urban Affairs

March 23, 1982

SUMMARY

I appreciate the opportunity to present before you the views of the AFL-CIO on H.R. 5731 and H.R. 5568. The AFL-CIO has been calling for actions to move the country out of the home building and financing crisis which is aggravating the national housing shortage, increasing unemployment, and prolonging the recession. Chairman Gonzalez and Chairman St Germain are to be commended for introducing these two bills which move in the right direction.

In H.R. 5731, continuation of loan guarantees for localities and of the Section 312 rehabilitation loan program, instead of allowing those programs to be phased out, will help to preserve urban neighborhoods and the older housing stock.

Title II of the bill provides necessary support for ongoing assisted housing programs and for programs that would help preserve the stock of assisted low-income housing. Thus, authority would be provided to support 19,000 new construction units under the public housing and Indian housing programs and an additional 16,000 units for the elderly and handicapped under the Section 202 program in fiscal year 1983. These programs serve the neediest low-income families and should be continued.

The provision of adequate operating subsidies and modernization authority for the public housing program represents a prudent policy. The old public housing projects, whose capital bonds have been amortized, provide low-income housing at a comparatively very low annual per unit subsidy cost.

Title II would also provide authority to support about 35,000 additional Section 8 existing housing units. In order to avoid inflationary pressures, such authority should be made available only in markets where there is an adequate supply of the size of units needed by families who would be eligible to receive existing Section 8 housing assistance in that community.

Moderate-income home ownership assistance is supported by authority for about 10,000 units under the regular Section 235 program for families with incomes up to 95 percent of the local median income. The home owner's effective interest rate may be paid down to as low as 4 percent.

The main new thrust for assisted housing production comes in a two-part program. Part A would permit activation of a Section 235(q) program, under which families with incomes up to 130 percent of local median income would be eligible. In 1980, based on the national median income, about a $27,000 income would be eligible. Payments by buyers could be as low as on a mortgage loan with an effective interest rate of 9½ percent. There would be $3.5 billion in budget authority to support the financing of an estimated 100,000 home ownership units, units with an average subsidy of $35,000 per unit over a ten year period.

Part B would be a new rental housing program, with subsidy assistance targeted to market areas of greatest need. A given amount of subsidy could be used flexibly by the state or local governments in a variety of delivery forms. Total budget authority of $1.3 billion would be authorized to support an estimated 50 to 100 thousand units. If 75,000 units were produced, the average per unit subsidy amount would be about $17,500 per unit over fifteen years. Twenty percent of the units, an estimated 15,000, would have to be reserved for families with incomes up to 80 percent below the local median. In 1980, the national average level of that income would have been $17,000. Part A and B, together, would provide an estimated 175,000 units of which 15,000 would be for those with incomes below 80 percent of median and 160,000 for people with higher incomes. Equity requires, and the AFL-CIO urges, that budget authority in support of Part B, for rental housing, should be increased substantially and made available for the lower income component.

Another area in which H.R. 5731 would halt the movement toward zero program levels is in rural housing. About 41,000 new construction units would be added under the low-income home ownership assistance program and about 16,000 under the low-income rural insured rental assistance housing program. Such program levels deserve full approval. There should be disapproval, however, of the Section 402 provision that would increase the percentage of income that must be paid as rent by a tenant in an assisted unit from 25 to 30 percent.

The proposed Emergency Mortgage Relief program in Title VI would help many unemployed home owners avert the loss of their homes. In a period of high and rising unemployment, with mortgage payments absorbing an unusually high proportion of income among younger home owners, the danger of widespread foreclosures is imminent. This is a reasonable program which would in all likelihood result in no cost to the government and would provide stability to a real estate market which otherwise could have a collapse in values that would destabilize the home building industry and the economy for many months to come.

One of the eligibility requirements of the mortgage relief program, however, is that mortgage payments must be at least 90 days delinquent. This should be changed to 30 days or 60 days, since there are a number of states in which mortgage foreclosure proceedings may be instituted when mortgage payments are delinquent far less than 90 days.

Enactment of the Home Mortgage Capital Stability Act (H.R. 5568) would be prudent in the national interest. It would provide assurance against a wholesale collapse of thrift institutions by providing them with guarantees of reserves equal to 2 percent of assets. This would prevent a loss of confidence in depository institutions and allow them to restructure their portfolio toward a more sustainable basis.

In order to discourage a reduction of the mortgage portfolio prior to the time that assistance by the institution is sought, at the end of the proposed subsection 13(h)(2)(C) of the Federal Deposit Insurance Act, the following proviso should be added: "provided that the percentage of assets consisting of such mortgages is not less than 80 percent of what was the comparable percentage on the effective date of the Home Mortgage Capital Stability Act."

One of the requirements for an institution that receives guarantees under the program is that not less than 50 percent of its annual net new deposits shall be used to issue mortgages. However, "net new deposits" would be defined "as determined by subtracting from deposits for each year the total amount of withdrawals and of interest and dividends credited each year." In tables for deposit flows of FSLIC-insured associations published regularly by the Federal Home Loan Bank Board, New Deposits Received minus New Deposits Withdrawn is shown as Net New Deposits Received, and the latter figure plus Interest Credited is shown as Net Deposit Gain. That accepted, appropriate concept of annual "net new deposits" should be used in determining the amount of funds that would become available for investment, stated as follows: "new deposits received plus amount of interst and dividends credited each year minus the total amounts of withdrawals." That would assure a more meaningful flow of available funds into residential mortgages than under the proposed definition. Otherwise, as indicated in details in my full statement, the assisted institutions could end up with no need to invest in mortgages, even in a year with a substantial positive net inflow of deposits.

Also, in order to fulfill the objective of aiding home building, the option for assisted institutions to meet one-half of their required mortgage investments through the purchase of mortgage backed securities, should be amended to provide that the mortgages collateralizing the securities, as well as the securities themselves, should have been originated after the effective date of the Home Mortgage Capital Stability Act.

With the recommended changes, H.R. 5568 would be an effective statute to sustain the viability of many troubled savings and loan associations for a period and support some revival of home building insofar as mortgage money would be made available for loans at about 12 percent interest rates. However, even at those interest rates, a high proportion of middle-income families could not afford to purchase homes. There is also a likelihood of a return to higher interest rates in the event of an incipient economic recovery.

There is no apparent willingness by the Administration or the Federal Reserve to supplement reliance on the tight-money, high interest rate policy, even though it has repeatedly led to more inflation, depression in home building, and economic recession. H.R. 5568 does not address itself to the broader problem of a credit policy to reduce interest rates, a necessity for adequate housing production and economic growth. The need for controlled credit availability without economically crippling interest rates can be addressed under the Credit Control Act of 1969 which presently is scheduled to expire at the end of June 1982. Since both the long-term viability of the thrift institutions and the ability of the housing industry to meet national housing needs can be affected by exercise of the authority in the Credit Control Act of 1969 and it is in the jurisdiction of your committee, I urge you to make permanent or extend that Act.

* * * * *

I appreciate the opportunity to present before you the views of the AFL-CIO on H.R. 5731 and H.R. 5568. They are much needed, positive initiatives to deal with the home building and home financing crisis which threatens to atrophy our housing supply and to lead to widespread financial instability, greater unemployment, and prolongation of the economic recession. The AFL-CIO has been calling for actions to counteract these trends and alleviate the social and economic hardship that has developed. Chairman Gonzalez and Chairman St Germain are to be commended for introducing the two bills which move in the right direction.

The Housing and Community Development Amendments of 1982 (H.R. 5731) would provide authority for a greatly needed positive program to stimulate production of decent housing for those who otherwise cannot afford it. The AFL-CIO has endorsed such housing production assistance to alleviate the worsening housing shortage and high unemployment caused by the continued depressed level of housing production. The bill would also provide continued authority for certain community development and housing rehabilitation activities that will help preserve neighborhoods. Finally, it would establish an Emergency Mortgage Relief program which is currently needed to prevent the loss of homes by thousands of home owners in this period of extended recession, high unemployment, and cutbacks in the number who may receive extended unemployment insurance payments.

Community Development

The continuation of authority in Section 101 for 1983 loan guarantees under Section 108(a) of the Community Development Act will facilitate public capital improvements by enabling cities to borrow in advance for property acquisitions with debt obligations to be repaid from enhanced tax revenues. It will support viable community development programs in a number of localities. Economic development at the local level will also be encouraged by authorizing the small amount made available to the Neighborhood Reinvestment Corporation to support a growing movement for neighborhood self-help economic development. The proposed authorization for continuation of Section 312 rehabilitation loans, in contrast to the Administration's proposal to terminate the program in fiscal year 1983, is a recognition of the need to provide assistance for the preservation of the existing housing stock. That is being accomplished under the Section 312 loan program through the below-market interest rate loans that are made available for housing occupied by people of limited income.

Ongoing Assisted Housing Programs

Title II of the bill provides necessary support for ongoing assisted housing programs and for programs that would help preserve the stock of assisted low-income housing. Thus, authority would be provided to support 19,000 new construction units under the public housing and Indian housing programs and an additional 16,000 units for the elderly and handicapped under the Section 202 program in fiscal year 1983. These programs serve the neediest low-income families and should be continued.

Because of the need and also because it represents a valuable public investment, the provision of adequate operating subsidies ($1.6 billion) and modernization authority ($1.7 billion) for the public housing program represents a prudent policy. Including any operating subsidies and modernization costs that have to be amortized, the old public housing projects whose capital bonds have been amortized, i.e., the mortgage has been paid off, provide low-income housing at a comparatively very low annual per unit subsidy cost.

Another authorization contained in Title II that would help preserve the existing housing stock would be the authority for operating assistance for troubled multifamily housing projects under assisted housing programs. The AFL-CIO also wishes to underline its strong endorsement for continuation of authority for GNMA special assistance and tandem plan mortgage commitments and purchases.

Title II would also provide authority that would support approximately 35,000 additional units under the Section 8 existing housing program, as well as about 76,000 to be converted from other assisted housing programs. At this point, I wish to jump ahead for a moment to a provision in the new Title III, Part B, Multifamily Housing Program. Under that program the Secretary of HUD is wisely directed to select projects for assistance on the basis of criteria which include "the extent to which the project or projects described in the application reduce the severe shortage of decent rental housing opportunities in the area for families and individuals without other reasonable and affordable housing alternatives in the private market." Those are also the types of markets in which it is counterproductive and creates inflationary pressures to increase effective demand for rental housing by issuing authority for leasing of existing units under the Section 8 program. In order to guide the Secretary to use his alternative program tools to fit local market conditions, the use of authority for existing Section 8 housing should also be conditioned on the basis of local market situations. Such authority should be made available only in markets where there is an adequate supply of the size of units needed by families who would be eligible to receive existing Section 8 housing assistance in that community. That requirement should be added by an appropriate amendment in Section 201.

Housing Production Programs

Title III contains authorization to support 10,000 more new home purchases by families with incomes up to 95 percent of median income under the regular Section

235 program which has an interest rate for the home buyer which may be as low as 4 percent. It will serve moderate-income buyers in need of housing.

The main new intiative for assisted low- and moderate-income housing production is also to be found in Title III of the bill. Title III, Part A of the bill would permit activation of the Section 235(q) home ownership assistance program by providing contract authority for annual payments up to an aggregate amount of $350 million for ten years and aggregate obligational budget authority of up to $3.5 billion. It is contemplated that the interest payments subsidies which would be made available with this contract authority would support the purchase of up to 100,000 homes. Eligible buyers could have incomes of up to 130 percent of the area median income. That would be about $27,000, based on a 1980 national median of $21,000. The subsidy could be used to reduce the payments that have to be made by the home owner for principal, interest, insurance, and taxes to that amount which the mortgagor would have to pay on a level payment, FHA-insured mortgage loan bearing a 9½ percent annual interest rate. The subsidy could not exceed the difference between the latter payment amount and the payment that would be required at the regular FHA mortgage interest rate, currently 15½ percent, or the difference between such payment and 25 percent of the mortgagor's income. A program of this type is desirable at this time to stimulate the production of housing which can meet middle-income needs.

A rental housing program is proposed in Part B of Title III. State or local government agencies would work with private developers under this program. The state or local government agencies would be the applicants for assistance for specific projects to be built. There will be a given amount of subsidy for a project which could be passed on to the developer in the form of a single capital grant, a loan, a rent subsidy to be used over time, or a loan for purchase of land. Local government contributions in kind or in cash would be encouraged, according to direction to the Secretary of HUD to give preference to project applications showing such local participation or other local contributions such as land or tax exempt financing. Funds would be targeted to areas with severe housing shortages, as indicated earlier. At least 20 percent of the units in a project would have to be kept available for occupancy of households with incomes that are not over 80 percent of the median. Referring again to the national family median income of $21,000 in 1980, twenty percent of the units would have to be reserved for families with incomes of up to about $17,000 on a national average, for a period of 15 years. There would be a total authorization of $1.3 billion and an estimate that with these funds the program could support 50,000 to 100,000 units depending on the various other factors involved. It should be noted that there is no income limitation for 80 percent of the unit occupants in the program although all units are to be for families or individuals without other reasonable and affordable housing alternatives in the private market.

Assuming for the moment that 75,000 units can be produced under the rental housing program, between the Title III home ownership and rental housing programs, a total of 175,000 assisted housing units could be supported of which approximately 15,000 would be for families with incomes below 80 percent of median, and 160,000 units would be for families with higher incomes. Under the rental housing program, again assuming 75,000 units, the average maximum per unit subsidy would be about $17,500 compared with $35,000 for the home ownership units. Assuming that for the 20 percent of units reserved for low-income families the average subsidy was about $20,000, it would leave an average of $15,000 for the remaining 60,000 rental housing units. We need both home ownership and rental types of housing for people who cannot afford to pay for decent housing. As a matter of equity, however, there should be an increase in authority for support of the rental housing program which would house at least some people with incomes below 80 percent of median. With additional assistance authority, it would be possible to require that a more significant percentage than 20 percent of the new rental program units should be occupied by people of lower income, and there would be a better possibility of producing 100,000 rental units instead of a possibility that only 75,000 would be produced. I strongly urge, therefore, that as a matter of need and equity there be additional authorization for the new rental housing program, to be added to the part that is reserved for households with incomes below 80 percent of median.

Rural Housing

Another area in which H.R. 5731 would halt the movement toward zero program levels is in rural housing. Title IV would provide authorization to support existing levels of effort for rural housing programs. This is in sharp contrast to the reduction of over 70 percent from 1982 recommended in the President's proposed budget for fiscal year 1983. Even the current program level for units that would be added by the bill would meet only a small fraction of the need for housing of low-income people in the credit-short rural areas served by Farmers Home Administration programs. About 41,000 new construction units would be added under the low-income home ownership assistance program and about 16,000 under the low-income rural insured rental assistance housing program. Such program levels deserve full approval.

There should be disapproval, however, of the Section 402 provision that would increase the percentage of income that must be paid as rent by a tenant in an assisted unit from 25 to 30 percent. The rationale given is to conform with requirements of HUD-assisted programs, but such conformity could be achieved by reverting to a 25 percent maximum in the HUD-assisted low-income programs. The latter course would offset some of the other take-backs from support for low-income people.

Title V contains the program extension authorization for FHA mortgage insurance programs and GNMA mortgage-backed security guarantees, both of which are needed to help finance housing in an uncertain credit climate.

Emergency Mortgage Relief

The proposed Emergency Mortgage Relief program in Title VI would help many unemployed home owners avert the loss of their homes. In a period of high and rising unemployment, with mortgage payments absorbing an unusually high proportion of income among younger home owners, the danger of widespread foreclosures is imminent. The delinquency loan ratio published by the Federal Home Loan Bank Board is already at a relatively high level. The foreclosure rate had been rising sharply in 1981. For example, the percentage of the number of mortgages held by FSLIC-insured savings and loan associations that were foreclosed during the first half of 1981 was .083 percent, up from .054 percent two years earlier. In terms of the number of foreclosures in these associations, the number of foreclosures in the first half of 1981 was 13,083 compared with 8,364 two years earlier.

The program of mortgage relief payments under Title VI would become effective when the Federal Home Loan Bank Board published delinquency ratio for amounts of outstanding mortgages 60 days delinquent averaged 1.3 percent or higher monthly for three consecutive months. It was above 1.3 percent in the last four months of 1981 and had been rising. Relief payments, that would be repayable loans, could be made only to owners who occupy a housing unit with a non-FHA-insured mortgage as their principal residence and who have incurred a large income drop through no fault of their own. (HUD can assist those with FHA-insured mortgages.) An eligible owner would have to be unable to correct the delinquency and resume full payment without assistance.

The HUD Secretary who would administer the program would have to determine that emergency payments are needed to avoid foreclosure and that the borrower would be able to resume full mortgage payments 24 months after assistance begins or when assistance ends; it could end after 12 months in the discretion of the Secretary. Another eligibility requirement is that mortgage payments must be at least 90 days delinquent. This should be changed to 30 or 60 days, since in some states foreclosure proceedings may be instituted after delinquency for such period. The assistance payments could be up to the amount of principal, interest, taxes, assessments, ground rent, hazard insurance, and lenders expenses in connection with payments or repayments. Under the program, the assisted home owner could be required to pay interest on funds loaned to him at a maximum rate equal to the rate on mortgages insured under the National Housing Act. The Secretary of HUD would have the right to foreclose and bid for purchase on any property in connection with assistance that has been provided. This is a reasonable program which would in all likelihood result in no cost to the government and would provide stability to a real estate market which otherwise could have a collapse in values that would destabilize the home building industry and the economy for many months to come.

The Home Mortgage Capital Stability Act

Enactment of the Home Mortgage Capital Stability Act (H.R. 5568) would be prudent in the national interest. It would provide assurance against a wholesale collapse of thrift institutions by providing them with guarantees of reserves equal to 2 percent of assets. This guaranteed safety margin would prevent a loss of confidence in depository institutions and allow them to restructure their portfolio toward a more sustainable basis. It would also be prudent because it would slow down the drain of funds from the insurance funds of the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation. In the process, specialized residential mortgage lending institutions would be kept operative and could help in restoring home building to a level that could begin to catch up with meeting the housing needs of the country. To help meet that objective, by facilitating a flow of funds that could be used in residential mortgage financing, certain amendments to the proposed legislation and related legislative actions will be recommended.

The Home Mortgage Capital Stability Act would avoid unnecessary federal outlays. Guarantees, payable only if failures occur, would be extended to those institutions that have a weakened capital base; that is, those with net worth equal to less than 2 percent of assets. Furthermore, they would have had to sustain losses recently for two consecutive quarters. Not less than 20 percent of the loan portfolio of a qualifying bank or savings and loan association could consist of mortgages secured by properties with one-to-four family units or by condominiums or cooperatives. In connection with the latter requirement, in order to discourage a reduction of the mortgage portfolio prior to the time that assistance by the institution is sought, at the end of the proposed subsection 13(h)(2)(C) of the Federal Deposit Insurance Act, the following proviso should be added: "provided that the percentage of assets consisting of such mortgages is not less than 80 percent of what was the comparable percentage on the effective date of the Home Mortgage Capital Stability Act."

Included among the other desirable features of H.R. 5568 are requirements that an institution being assisted would have to provide quarterly reports on condition to the lending agency; and during the period in which it has a guarantee in effect, not less than 50 percent of its annual net new deposits shall be used to issue mortgages. However, "net new deposits" would be defined "as determined by subtracting from deposits for each year the total amount of withdrawals and of interest and dividends credited each year." In tables for deposit flows of FSLIC-insured associations published regularly by the Federal Home Loan Bank Board, New Deposits Received less deposits withdrawn is shown as Net New Deposits Received, and the latter figure plus Interest Credited is shown as Net Deposit Gain. There would seem to be no justification for subtracting the amount of interest and dividends credited during the year, which become deposit account funds available for loans. The accepted, more appropriate definition of annual "net new deposits" for determining the amount of funds that would become available for investment would be "new deposits received plus amount of interest and dividends credited each year minus the total amounts of withdrawals." That would assure a more meaningful flow of available funds into residential mortgages than under the proposed definition, which would subtract instead of adding a substantial amount of new loanable funds. Such funds should be included among net new deposits, of which 50 percent would have to be used to issue new residential mortgages.

The difference in definitions would make a tremendous difference in the base for required mortgage investment by assisted institutions. To illustrate, in 1980, all FSLIC-insured savings and loan associations had the following experience, as published by the Federal Home Loan Bank Board:

New Deposits Received	$424,177,000,000
New Deposits Withdrawn	413,509,000,000
Net New Deposits Received	10,668,000,000
Interest Credited	30,288,000,000
Net Deposit Gain	40,956,000,000

If all of the insured associations had received assistance under H.R. 5568 in 1980, with the definition of "net new deposits" proposed therein, the net new deposits would have been negative (-$19.6 billion), and the associations would not have been required to invest any funds in residential mortgages. On the other hand, if the accepted, more logical definition were used, the associations would have had to invest 50 percent of almost $41 billion in residential mortgages. The proposed definition of "net new deposits" should be changed to the accepted definition that I have indicated, which is the same as the one that has been used traditionally by the Federal Home Loan Bank Board.

The bill would also require that the mortgages to be made with the 50 percent of new net deposits should be secured by either one-to-four family residential structures or individual units in a condominium or cooperative project and that it be made to first-time home buyers. The mortgages also would have to be made bearing an interest rate not greater than 1 percent above the average cost of funds to the institution and in amount no greater than the amount permitted in the regular Section 203 FHA-insured home loan program.

It is understandable and desirable that the mortgage loans to be made should be restricted as to amount and interest rate spread so that they can serve first-time home buyers. However, many younger families in need of housing will not be able to afford to own a home even under such terms and will be seeking rental housing. There is also a great shortage of rental housing in many areas and a continuing increase in conversions of apartments to condominiums which restricts the rental housing supply. In the interest of encouraging a more balanced composition of housing production and supply, it is recommended that an institution receiving assistance should also be permitted to use up to 25 percent of its net new deposits to finance multifamily housing projects which would provide rental units with monthly rentals comparable to monthly housing expenditures that would be required for the type of single-family units to be provided for first-time home buyers.

The fulfillment of a requirement that an assisted institution must devote 50 percent of its net new deposits to residential mortgages is greatly diluted by the proposed subsection 13(h)(2)(E)(iv) of the FDIC Act. This would permit an assisted institution to satisfy up to 50 percent of the required mortgage lending by purchasing mortgage backed securities which have been issued after the date on which the assisted institution receives assistance. While the securities would have to have been issued after that date, there is no requirement that the mortgages against which the securities are issued should have been issued after that date. Consequently, the assisted institution investing in such mortgage-backed paper may be purchasing paper that was secured by mortgages issued in prior years that would not necessarily contribute to support for additional residential mortgage financing. It could result in only 25 percent of the net new deposits being used for mortgage financing which would support additional housing.

It is recommended, therefore, that in the aforementioned clause (iv) after the word "securities" the balance of the clause be changed to read: "issued after the date on which the insured bank receives assistance under this subsection for the first time and backed by mortgages described in clause three that were made after that date."

Changes similar to all of the aforementioned recommended changes should also be made in section 2(b) of the bill dealing with amendments to the National Housing Act which would be applicable to institutions insured by the Federal Savings and Loan Insurance Corporation.

The FDIC or FSLIC would purchase from an assisted institution capital notes bearing an interest rate related to the average yield on Treasury securities of comparable maturities. This should provide the institutions with a lower rate than when borrowing from Federal Home Loan banks and facilitate a profitable operation.

With the recommended changes, H.R. 5568 would be an effective statute to sustain the viability of many troubled savings and loan associations for a period and support some revival of home building insofar as mortgage money would be made available for loans at about a 12 percent interest rate.

However, even at those interest rates, a high proportion of middle-income families could not afford to purchase homes. There is also a likelihood of a return to higher interest rates in the event of an incipient economic recovery. This would raise the cost of money to thrift institutions and lead to higher mortgage interest rates even among assisted institutions. Furthermore, the institutions that do not need assistance, as well as various other sources of funds, would most likely demand higher mortgage interest rates as market interest rates rose.

There is no apparent willingness by the Administration and Federal Reserve to supplement the tight-money, high interest rate policy of fighting inflation, even though it repeatedly leads to more inflation, depression in home building, and economic recession. H.R. 5568 does not address itself to the broader problem of a credit policy to reduce interest rates. The broader problem of controlled credit availability without economically crippling interest rates can be addressed under the Credit Control Act of 1969 which presently is scheduled to expire at the end of June 1982. The implementation of credit control authority in 1980 helped to bring interest rates down rapidly, to reverse a decline in home building, and to get economic recovery under way. Other countries have successfully used similar credit regulation. Since both the long-term viability of the thrift institutions and the ability of the housing industry to meet national housing needs can be affected by exercise of the authority in the Credit Control Act of 1969 and it is in the jurisdiction of your full committee, I urge you to act to make permanent or extend that Act.

Chairman GONZALEZ. Thank you very much, Mr. Schechter. We next recognize Mr. Weiner.

STATEMENT OF LEON N. WEINER, PRESIDENT, NATIONAL HOUSING CONFERENCE

Mr. WEINER. Thank you, Mr. Chairman, and thank you, Congressman Evans. We come from the little State of Delaware where we have had to live and work. It is smaller than many suburbs of New York City or even burroughs of New York City, in terms of population.

Mr. SCHUMER. You are getting all of our banks.

Mr. WEINER. We are trying hard to get banks. We are going to Massachusetts and Maryland.

Mr. MITCHELL. You have been forbidden to cross the border into the State of Maryland, so do not bother.

Mr. WEINER. It is very difficult to get from Delaware to Washington unless I go through Maryland, Congressman Mitchell.

Mr. MITCHELL. That is the idea.

Mr. WEINER. I would say that Congressman Evans is serving in the best traditions. He has been, for a long time, the minority side of the Housing Subcommittee. I think of Congressman Widnall and the tremendous contributions that he made, and Congressmen Stanton and Green and others, who have really been concerned with housing.

He indicated that I was a Democrat and he was a Republican. I would like to just simply modify it a little bit. My politics is housing and has been housing for the last 35 years, and I certainly support Republican or Democratic proposals and Congressmen who are concerned with the questions of housing, and I think Tom knows that, as do many others.

I am here before you as president of the National Housing Conference. I have with me Bob Malakoff, who is our newly elected national executive vice president. Some of you may have known Mr. Malakoff when he served over on the staff of the Housing Subcommittee in the U.S. Senate, and we are delighted to have him. And Carl Coan, who has been our legislative counsel.

I will not go into an elaboration of what the National Housing Conference is, because I think most of you know that it is a broad umbrella organization that has been active in the field of housing for a long time.

In the interest of brevity, Mr. Chairman, I am going to read my remarks.

Chairman GONZALEZ. Certainly. Without objection, so ordered.

Mr. WEINER. And if I appear to be low keyed, as I was criticized for being, on a program with Congressman Schumer on the McNeil-Lehrer show, they told me that I was extremely low-keyed and they thought the fire had gone out. Let me simply say the situation is just that grave that I think it cannot be handled with the usual vigor and needs to be looked at a little more seriously.

The hearings are being held, as you know, at a time of considerable distress in the economy in general and for housing in particular. The Nation is in a serious recession and housing is in a depression and we have been there since 1979, when the Federal Reserve

Board did that magic jump of 1 percent in its discount rate on that famous Black Friday, October 6. In fact, the housing industry is probably in its worst condition since the 1930's, with housing starts for 7 months in a row under 1 million units on an annualized basis and for most of that time under 900,000 units.

At the same time, we have a great pent-up demand for both ownership and rental housing, which is going unmet. Those most affected by this situation are those least able to afford it, the Nation's low- and moderate-income families and the elderly.

Construction unemployment is approaching 20 percent. Some of the statistics from the State of Delaware on housing starts for the first 2 or 3 months of 1982 are absolutely shocking, because in 1980, for example, there were about 200 units in the first 2 months, and in 1981 there were about 130, and right now there are 30 units. Thirty permits that have been taken out for starts in the entire State.

Builders of housing of all types are going broke by the hundreds. Many families are finding it increasingly difficult to keep their mortgage payments up, as delinquencies have risen significantly in recent months.

Normally, when things turn this bad in the economy, and in housing especially, the Federal Government undertakes to resuscitate housing and, through it, the economy in general, and calls on the housing industry to lead us out of a recession. Unlike the past recessions since World War II, we have yet to see any such effort to remedy today's problems, although the beginnings are appearing in the Congress itself.

The administration so far has only proposed or undertaken actions which, frankly, at this point would further depress the housing industry. They have announced plans to reduce the present pipeline—the word was eliminate rather than reduce; a little stronger I believe—of approved but uncompleted low- and moderate-income housing units by 300,000, and HUD has undertaken a series of administrative actions to assure that this 300,000-unit reduction is accomplished.

The very limited amount of housing assistance approved in the HUD Appropriations Act for this fiscal year would also be decimated by the administration, which is seeking a rescission of $9.4 billion in budget authority and proposing to use over $7 billion of fiscal 1982 budget authority to switch existing rent supplement units to the section 8 program, whether needed or not. The result of all of this, if approved by the Congress, would be practically no addition to the supply of housing for the lower income people.

The administration has also proposed practically no additional housing assistance for fiscal year 1983, but instead has indicated it will seek a further rescission. It has further announced its intention to seek substantial cutbacks in rural housing and in the basic FHA and GNMA programs.

It was in this atmosphere of retreat, from a 50-year history of affirmative Federal efforts to improve the housing of the American people, that the National Housing Conference held its 51st annual meeting last week. The conference was formed in 1931, specifically to work for the achievement of the opportunity of a decent home for every American. And incidentally, in our founding we were stimulated by that now-famous housing conference that President Herbert Hoover called on December 4, 1931.

Because Mr. Hoover recognized the nature of the crisis, the need for housing for the American people, the need for doing something about it, the seeds of the Home Loan Bank Board Act were brought forth from that conference—ultimately, FHA public housing and a whole series of programs. We cannot seem to learn from the history of 50 years ago and seem to be going down that same path of trying to get Federal participation completely out of the field of providing shelter for the American people.

This became a national housing policy in 1949 in that year's housing act, and has been reaffirmed by Congress several times since. While efforts to meet that goal have had their ups and downs over the past 30 years, never have we seen such a calculated plan to withdraw from this Federal commitment, as has now been laid before the Nation.

The National Housing Conference, therefore, in its resolutions adopted last week, called for a recommitment from the Federal Government to an active role in housing and to meeting the housing needs of this Nation. We also recognize that we are faced with a period of severe budgetary constraints and with projected deficits in the $100-billion-plus range, deficits which just a few years ago would have been unimaginable and, therefore, have structured our proposals accordingly.

The resolutions and a statement on the 1982 housing crisis adopted at our annual meeting are attached. And we would like to submit those for the record. You will note that the resolutions basically call for maintaining the very minimal level of assistance contained in the HUD and the Farmers Home Appropriation Acts for this year, and continuing at at least that level in fiscal year 1983. These levels are far less than what is needed, but at least they represent a recognition that we must continue to endeavor to meet the housing needs of those with low and moderate income.

Our resolutions also call for the Federal Government to undertake such other actions and efforts as may be needed to assure an adequate flow of mortgage credit at affordable interest rates. And I do not mean 17 percent and I do not mean 15 percent, and I do not mean 13 percent. What is affordable at this point, if we are going to house any proportionate share of the American people, is that we have to see interest rates come down to 8 and 9 percent, where they can match the incomes and the ability of people to pay. There is a great deal of doubt whether we are going to see them ever get down that low.

Whatever reduction in interest rates that will take place, it is of absolute critical concern that there be one; I am not going to address some of the other questions which I just heard Dr. Schechter introduce—but certainly, I believe some of them make a lot of sense in terms of looking at the problem.

I will not try to list each of the resolutions. However, I would like to highlight some of their major features. There are a number of other policies that the housing conference has stood for, and for the first time in 50 years we are not handing out an encyclopedia of 150 or 200 pages listing all of our policies. Policies such as our strong commitment to affirmative action and toward open occupancy and freedom of choice; policies calling for meeting our national housing goals and of qualifying or specifying what they are, and so forth, still remain part of our overall program, although we recognize the fiscal restraints.

First and most important, we urge the Congress to reject the proposed rescission of funds appropriated for fiscal year 1982. Second, we urge the Congress to take such actions as may be necessary to permit construction to start on the tens of thousands of section 8 and other HUD-assisted housing units, which are ready to go to construction but cannot because of a lack of affordable mortgage financing and outrageously high interest rates now confronting housing.

If this means that additional GNMA tandem funds must be provided, then we urge that those funds be provided now for at least all of those projects which participated in the recent lottery held by GNMA and failed to be funded. This would permit construction of almost 60,000 units to get underway within 2 to 3 months of the funds being provided. And I do not need to spell out for you what that would mean in terms of reducing the unemployment in construction, or starting to reduce that unemployment, and getting the guys back to work.

We also urge that, if HUD is unable or unwilling to make reasonable adjustments to its financing adjustment factor regulations for those section 8 projects planning to use tax-exempt financing, Congress make those adjustments for HUD. At a minimum, the present June 1, 1982, start of construction date must be extended to at least the end of the fiscal year and an interest rate of up to 14 percent should be authorized for the FAF. It seems to me that the free market is simply telling us that the present 12-percent limit is not going to work. If we believe in the free market and if we believe in supply-side economics, then I think certainly, we need to take a good look at that one.

Congress should further direct HUD to cease its arbitrary administrative actions designed to kill section 8, existing section 8, and public housing projects. These actions have taken the form of unrealistic deadlines for the commencement of construction, deadlines which do not recognize the realities of the mortgage market; of refusal to recognize real cost increases since funds were first reserved for a project, but instead to permit only an arbitrary 7¾ percent annual cost increase; and even of refusing to permit reserved funds to be switched from one reservation category to another, where financing might be more feasible.

I would just suggest that we look at the Defense Department and its M–1 tank. When it discovered that the tank had too fragile a transmission system, it found it necessary to build a bulldozer that would run along with that tank in order to dig a hole for the tank when it got up to the front lines, that I know a little bit about bulldozers; since I happen to be a builder and in construction all my life.

In 1978, the bulldozer cost $200,000. In 1981, last year, it had risen to $900,000. I see by the papers last week that that bulldozer is now $1.25 million. I have not heard anybody screaming about the kind of cost overruns that the Defense Department continues to ask for. At the same time, they are trying to limit us to a 7¾-percent annual cost increase, during this high inflationary period when the cost of construction went through the ceiling.

I think it is clearly and obviously a method to justify the statement that we want to fund the entire pipeline if it is economically feasible. It is not economically feasible at a 7¾-percent annual rate, if you are sitting with a section 8 job that has been waiting for 3 years to get either zoning or to get HUD approvals or to wait until the FAF was approved last year, which took almost a year, or which sweated it out in a lottery for the existing GNMA funds.

In the situation of switching funds to another category, the premise is that HUD's computer is set up so as to count the switch as a cancellation in the first category and the authorization of new units in the second category, which would be contrary to HUD's promise to OMB not to authorize any new section 8 units. In other words, HUD seems dedicated to not producing housing, not finding ways to make things work in these very difficult times.

We also call in our resolutions for continued funding of present housing programs in 1983, at least at the levels approved for 1982. That is, without the rescissions. We recognize that some have raised questions about the efficacy of many of the existing housing assistance programs. We also recognize that there are various proposals floating around to switch housing assistance to a voucher program or to a block grant program, or to some other method which allegedly will be less costly than the present methods.

I heard the HUD General Deputy Assistant Secretary for Housing, speaking to a public housing group last year, appeal to the people who were in the development of public housing, "Why don't you keep the cost of public housing down to the section 8 cost of construction?" I thought it was a very, very beautiful note to point out that somewhere or other we get very confused when we talk about what programs we are involved in.

We sympathize with efforts to reduce, where reasonably possible, the cost of assisted housing. But, we strongly oppose stopping present programs until new and effective replacement programs are developed and operational. Many of the members of this committee, who have been here for a while, know that from the day a new program is authorized, from the day the money is allocated, that it will take 4, 5 years before we learn how to wrestle with it, how HUD people can make it work in terms of their processing, and how the private sector can finally bring it into the field.

Unfortunately, the administration has not yet come forward with the particulars of its housing legislative proposals for this year, other than we know they are talking about vouchers. We do, however, know from its budget proposals what the basic premises are on which this legislation will be based. We reject those premises as totally inadequate.

The limited housing voucher program outlined in the administration's budget proposals will not meet the housing needs of the low income, nor will the limited rehabilitation grant program it has proposed. While each of them has a place in the overall scheme of constructively trying to deal with the question of housing, they cannot be considered a basic housing policy.

A complete cessation in new construction and substantial rehabilitation of housing for the low- and moderate-income people just does not make sense at this time of historic lows in the vacancy rate for rental housing. This is especially true in the rural areas, where vacant housing is usually nothing better than a shack without plumbing or other modern and necessary amenities. Therefore, we urge the subcommittee to authorize at least the same level of housing loans and grants for the Farmers Home Administration's programs as were provided this fiscal year.

To call for a reduction in the use of FHA and GNMA programs in this time of low housing production and low housing sales just does not make sense. Instead of constraining these proven aids to the housing market, we believe that the administration and the Congress should be seeking ways to make them work more effectively and structuring special programs to increase the production of much needed housing. We therefore support programs which would spur the production of single family homes and/or multifamily projects for the moderate and middle income, but not at the expense at this time of further reducing assistance for the lower income.

In this vein, we should like to express our general support for the provisions of H.R. 5731 introduced by the chairman and 18 other members of the subcommittee, with one basic reservation. H.R. 5731 would basically continue the housing and community development programs at the constrained budget levels approved for this year. This we endorse. It would also authorize assistance for two new programs. The first of these would be a one-time infusion of funds into single-family production through 235(q), to help get that industry off its back. We support that effort.

The other new program would be initiation of an ongoing program to increase the supply of rental and cooperative housing. We support such an effort, and we support the concept of requiring that 20 percent of the units be reserved for the lower income. And may God help us to try to make it work in the field, because, while I support the concept, I have to tell you I am not sure where we can get the mirrors to do it with at the moment.

I am looking forward to how it will work out in real life, when you have to put it into production and into the field.

On the other hand, we are concerned that the low-income housing that would be provided under this program not be looked upon as a replacement for section 8, until it is known whether this new program will in fact work, and until it is functioning and actually producing housing.

In closing, I would like to say that the housing conference will continue its dedication to working for the achievement of a decent home and a suitable living environment for every American, as called for by Congress in 1949. We urge the subcommittee, the full Banking Committee, the House, and the whole Congress to rededicate themselves to achieving that goal, to help fight against the retreat from that goal that now seems to be under way.

We have helped set up the save housing coalition, and I am proud to see the chairman wearing one of the buttons. We are delighted that he was able to come to our convention, at which time the save housing coalition really got started. The coalition was formed last week, and includes, at least at this time, 20 leading organizations from all walks of housing and housing-related interests.

I have attached for your information the coalition's statement of purpose and a list of the participating organizations.

I want to finish by stressing four matters. One, housing has been cut disproportionately. It has taken a more critical cut in the budget than almost anything else, and I certainly support the concern for the total budget. Housing has been whacked to the point where I think we have to say stop, get the cuts somewhere else. Last year, all of us stood silently in support of a program of attempting to establish some kind of constraints, but we think it has now reached the limit.

Second, housing programs mean jobs and employment, and bringing the housing industry back into production will affect a large circle of other industries. That is important.

Third, the low income are being forced to undergo disproportionately large rent increases by shifting them from 25 to 30 percent of income. Many of these people are minorities. Mostly they are people who can least afford a decrease in assistance, particularly in public housing where they are now going to count food stamps as part of their income.

Finally, the private homebuilding industry is being driven out of the programs by the proposals to rescind the funds and the obligations as a result of these search and destroy tactics.

I want to say in my last sentence, and this is not as president of the housing conference. I happen to be a builder and developer. I will think twice before relying on the Federal Government or the State government or anybody else on any promise to go out and build housing for low- and moderate-income families or anybody else.

I have in the field close to $1.1 million invested in land, in engineering, in architectural drawings, in commitments that we have paid and are now being told that there aren't enough units, that the fund reservations cannot be amended, and there isn't going to be the opportunity to fund those units, and so on. From Seaford, Del., to New London, Conn., we are sitting in a state of suspension. We were asked to go out and build mixed units, 20 percent section 8, mix them with 80 percent at market rent. And we were told that we would have tandem money in order to make it market feasible. There is none.

Why should the private sector have any confidence at all in the Federal Government? If the Federal Government made that kind of commitment to the industrial military defense industry, they wouldn't sit still for a second. Maybe they are banking on the fact that we are all a bunch of small businessmen. Maybe they are banking on the fact that we are not going to sue, and are not going to strike back. Maybe they are banking on the fact that after all, it is for low-income people, and maybe they are not going to strike back.

I am a conservative. I am a real conservative. I want to conserve the capitalist system. It has been good to all of us. I want to conserve this political democracy that we have in the United States, and I want to be sure that in that conservation effort we don't breed the seeds of revolt, of unhappiness, and of dismay and distress for the people who need housing the most.

Thank you, Mr. Chairman.

[Mr. Weiner's prepared statement, with attachments, on behalf of the National Housing Conference, follows:]

STATEMENT
OF
THE NATIONAL HOUSING CONFERENCE
BEFORE THE
SUBCOMMITTEE ON HOUSING AND COMMUNITY DEVELOPMENT
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
UNITED STATES HOUSE OF REPRESENTATIVES

March 23, 1982

My name is Leon N. Weiner and I appear here today as President of the National Housing Conference. We appreciate this opportunity to present our views on housing legislation for 1982.

These hearings are being held at a time of considerable distress in the economy in general and for housing in particular. The nation is in a serious recession and housing is in a depression. In fact, the housing industry is probably in its worst condition since the 1930's, with housing starts for seven months in a row under a million units on an annualized basis, and for most of that time under 900,000 units.

At the same time we have a great pent-up demand for both ownership and rental housing, which is going unmet. Those most affected by this situation are those least able to afford it, the nation's low and moderate income families and elderly.

Construction unemployment is approaching 20%, over double that for the nation as a whole. Builders of housing of all types are going broke by the hundreds. Many families are finding it increasingly difficult to keep their mortgage payments up, as deliquencies have risen significantly in recent months.

Normally, when things turn this bad in the economy, and in housing especially, the Federal Government undertakes to resuscitate housing and through it the economy in general. Unlike past recessions since World War II, we have yet to see any such effort to remedy today's problems. The Administration so far has only proposed or undertaken actions which would further depress the housing industry.

The Administration has announced that it plans to reduce the present pipeline of approved, but uncompleted, low and moderate income housing units by 300,000 and HUD has undertaken a series of administrative actions to assure that this 300,000-unit reduction is accomplished. The very limited amount of housing assistance approved in the HUD Appropriations Act for this fiscal year would also be decimated by the Administration, which is seeking a rescission of $9.4 billion in budget authority and proposing to use over $7 billion of FY1982 budget authority to switch existing rent supplement units to the Section 8 program, whether needed or not.

The result of all this, if approved by the Congress, would be practically no addition to the supply of housing for the lower income. The Administration has also proposed practically no additional housing assistance for FY1983, but instead has indicated it will seek a further rescission. It has further announced its intention to seek substantial cutbacks in rural housing and in the basic FHA and GNMA programs.

It was in this atmosphere of retreat, from a 50-year history of affirmative Federal efforts to improve the housing of the American people, that the National Housing Conference held its 51st Annual Meeting last week. The Conference was formed in 1931 specifically to work for the achievement of the opportunity of a decent home for every American. This became a national policy in 1949 in that year's housing act and has been reaffirmed by Congress several times since. While efforts to meet that goal have had their ups and downs over the past 30 years, never have we seen such a calculated plan to withdraw from this commitment as has now been laid before the nation.

The National Housing Conference, therefore, in its resolutions adopted last week called for a recommitment from the Federal Government to an active role in housing and to meeting the housing needs of the nation. We also recognize that we are faced with a period of severe budgetary constraints, with projected deficits in the $100 billion plus range, deficits which just a few years ago would have been unimaginable, and, therefore, have structured our proposals accordingly.

The resolutions and a statement on the 1982 Housing Crisis adopted at our Annual Meeting are attached. You will note that the resolutions basically call for maintaining the very minimal level of assistance contained in the HUD and FmHA appropriations acts for this year and continuing at least that level in FY1983. These levels are far less than what is needed, but at least they represent a recognition that we must continue to endeavor to meet the housing needs of the low and the moderate income.

Our resolutions also call for the Federal Government to undertake such other actions and efforts as may be needed to assure an adequate flow of mortgage credit at affordable interest rates, so as to permit the housing industry to get up off the floor and produce the housing that Americans of all income levels unquestionably need. I will not endeavor to list each of the resolutions adopted by NHC last week. However, I should like to highlight some of their major features.

First, and most important, we urge Congress to reject the proposed rescission of funds appropriated for FY1982. Secondly, we urge the Congress to take such actions as may be necessary to permit construction to start on the tens of thousands of Section 8 and other HUD-assisted housing units, which are ready to go to construction but cannot because of a lack of affordable mortgage financing and the outrageously high interest rates now confronting housing.

If this means that additional GNMA Tandem funds must be provided, then we urge that those funds be provided now for at least all those projects which participated in the recent lottery held by GNMA and failed to be funded. This should permit construction of almost 60,000 units to get underway within two to three months of the funds being provided.

We also urge that, if HUD is unable or unwilling to make reasonable adjustments to its financing adjustment factor regulations for those Section 8 projects planning to use tax-exempt financing, Congress make those adjustments for HUD. As a minimum, the present June 1, 1982, start of construction date must be extended to at least the end of the fiscal year and an interest rate of up to 14% should be authorized for the FAF.

Congress should further direct HUD to cease its arbitrary administrative actions designed to kill existing Section 8 and public housing projects. These actions have taken the form of unrealistic deadlines for the commencement of construction, deadlines which do not recognize the realities of the mortgage market; of refusal to recognize real cost increases since funds were first reserved for a project, but instead to permit only an arbitrary 7-3/4% annual cost increase; and even of refusing to permit reserved funds to be switched from one reservation category to another where financing might be more feasible.

In the last situation the premise is that HUD's computer is set up so as to count the switch as a cancellation in the first category and the authorization of new units in the second category, which would be contrary to HUD's promise to OMB not to authorize any new Section 8 housing units. In other words, HUD seems dedicated to not producing housing, not to finding ways to make things work in these difficult times.

We also call in our resolutions for a continued funding of present housing programs in FY1983 at least at the levels approved for FY1982. We recognize that some have raised questions about the efficacy of many of the existing housing assistance programs. We also recognize that there are various proposals floating around to switch housing assistance to a voucher program or to a block grant program or to some other method which alledgedly will be less costly than present methods. We sympathize with efforts to reduce, where reasonably possible, the cost of assisted housing. But, we strongly oppose stopping present programs until new and effective replacement programs are developed and operational.

Unfortunately, the Administration has not yet come forward with the particulars of its housing legislative proposals for this year. We do, however, know from its budget proposals what the basic premises are on which this legislation will be based. We reject those premises as totally inadequate. The limited housing voucher program outlined in the Administration's budget proposals will not meet the housing needs of the low income. Nor will the limited rehabilitation grant program it has proposed.

A complete cessation in new construction and substantial rehabilitation of housing for the low and moderate income just does not make sense at this time of historic lows in the vacancy rate for rental housing. This is especially true in rural areas where vacant housing is usually nothing better than a shack without plumbing or other modern and necessary amenities. Therefore, we urge the Subcommittee to authorize at least the same level of housing loans and grants under the Farmers Home Administration's programs as were provided this fiscal year.

To call for a reduction in the use of FHA and GNMA programs in this time of low housing production and low housing sales just does not make sense. Instead of constraining these proven aids to the housing market, we believe that the Administration and Congress should be seeking ways to make them work more effectively and structuring special programs to increase the production of much needed housing. We, therefore, support programs which would spur the production of single-family homes and/or multifamily projects for the moderate and middle income, but not at the expense of further reducing assistance for the lower income.

In this vein we should like to express our general support for the provisions of H.R.5731, introduced by the Chairman and 18 other members of the Subcommittee, with one basic reservation. H.R.5731 would basically continue the housing and community development programs at the constrained budget levels approved for this fiscal year. This we endorse. It would also authorize assistance for two new programs. The first of these would be a one-time infusion of funds into single-family production through 235(q) to help get that industry off its back. We support that effort.

The other new program would be initiation of an ongoing program to increase the supply of rental and coopeative housing. We support such an effort and we support the concept of requiring that 20% of those units be reserved for the lower income. On the other hand, we are concerned that the low-income housing that would be provided under this program not be looked upon as a replacement for the Section 8 program, until it is known whether this new program will in fact work and until it is functioning and actually producing housing. We have learned too often over the years that it takes a substantial time period for any new HUD program to be put in place and for HUD personnel and those who will use that program to learn how the program functions. We do not believe it is right that a working program such as Section 8 be stopped until a new program is fully underway.

In closing, I should like to say that the National Housing Conference shall continue its dedication to working for the achievement of "a decent home and a suitable living environment for every American" as called for by Congress in 1949. We urge this Subcommittee, the full Banking Committee, the House and the whole Congress to rededicate themselves to achieving that goal.

To help fight against the retreat from that goal that now seems to be underway, we have helped set up the Save-Housing Coalition. This coalition was formed last week and it includes at this time 20 leading organizations from all walks of housing and housing-related interests. I have attached for your information the Coalition's statement of purpose and a list of the participating organizations. We urge you to join with us in working "to preserve this nation's commitment to the goal of decent, affordable housing for all Americans."

RESOLUTIONS
# of the
NATIONAL HOUSING CONFERENCE

March 1982

Preamble

The National Housing Conference, dedicated to the goal of meeting the housing needs of the nation, reaffirms its purpose and calls upon the Congress and the Administration this year to pursue a program which will serve these needs.

Housing is a national concern. The Conference strongly opposes all steps to shed the nation's traditional responsibilities and commitments in this field .

It is not enough to say that the nation as a whole is better housed than it was fifty years ago, when we know that at least eight million rural and urban families continue to reside in substandard and overcrowded housing. That there are no bread lines today does not mean there is no need; nor does it justify the failure to anticipate the exigencies of tomorrow.

This nation's housing stock is not forever: it requires constant replenishment, improvement and rehabilitation. Today, abandonment and deterioration threaten to out-strip new construction. The costs of owning or renting housing are outdistancing the ability of all to pay: young families, the elderly, the poor and the not-so-poor. It is the responsibility of the Congress and the President to respond to these conditions and to marshall the resources of the nation to recommit the federal government to an active role in housing.

The National Housing Conference supports budgetary and other actions which will permit the goals stated in the following resolutions to be achieved. These resolutions have been formulated with current budgetary constraints in mind and do not incorporate all desirable measures to meet this nation's housing needs. Nor do they identify all of the tools which may be available to achieve these goals. Rather, they address only the most fundamental needs which must be served on a continuous and uninterrupted basis and reflect objectives which set the parameters for essential action by the federal government now and in the coming fiscal year.

THE NATIONAL HOUSING CONFERENCE RESOLVES TO:

IMMEDIATE RELIEF

1. OPPOSE current Administration policies which would thwart the will of Congress by eliminating the construction of 300,000 units of previously committed low and moderate income housing.

2. SUPPORT the extension of the Financing Adjustment Factor for tax-exempt, Section 8 financing through the remainder of FY 1982 at a rate not to exceed 14%, and an emergency supplemental appropriation to fund the FAF.

3. SUPPORT the supplemental appropriation of sufficient tandem funds to finance projects which have been committed and not funded.

4. SUPPORT the indefinite extension of the March 31, 1982 deadline for using authorized, appropriated and uncommitted funds under the Section 235 home ownership program.

5. OPPOSE the rescission of nearly $10 billion of Section 8 and public housing funds approved in the Appropriations Act for FY 1982.

6. OPPOSE the use of $7.15 billion of FY 1982 Section 8 and Public Housing New Construction funds to convert rent supplement and 236/RAP units to Section 8 existing contracts.

FY 1983 DIRECT ASSISTANCE FUNDING LEVELS

7. SUPPORT funding of Public Housing, Indian Housing and Section 8 New Construction/Substantial Rehabilitation at least at the level approved in the Appropriations Act for FY 1982 ($9.55 billion).

8. SUPPORT funding of the Section 8 Existing Program at least at the level approved in the Appropriations Act for FY 1982 ($7.82 billion).

9. OPPOSE the enactment of a voucher program replacing the present Section 8 Existing Housing Program, until details of a voucher program are available and it can be determined that such a program will provide benefits at least equal to those under the existing Section 8 Program.

10. SUPPORT funding of rural housing programs sponsored by the Farmers Home Administration at least at the FY 1982 levels (Section 502, Home Ownership Loans, $2.73 billion; Section 515, Rural Rental Housing $940 million; Rental Assistance, $398 million; Farm Labor Housing, $38.8 million; and Self-Help Housing, $6 million).

11. SUPPORT the funding of the Section 202 program for housing for the elderly or handicapped at least at the FY 1982 appropriations level ($799.2 million).

12. SUPPORT the adoption of a shallow-subsidy, moderate-income multifamily rental housing production program at the level of at least 100,000 units.

13. SUPPORT the adoption of a shallow-subsidy, moderate-income, single-family homeownership housing production program at the level of at least 100,000 units.

LOW-INCOME RENTS

14. OPPOSE the increases in rents proposed for tenants in low-income rental housing projects assisted by HUD and FmHA and provide authority for such additional subsidy as is necessary.

15. SUPPORT the restoration of the historic 25% rent-to-income ratio for tenants of assisted housing.

16. SUPPORT the restoration of the historic income limit of 80 percent of median for Section 8 and public housing.

PUBLIC HOUSING STOCK

17. SUPPORT funding of the public housing modernization program at least at the FY 1982 level ($90 million).

18. SUPPORT the provision of operating subsidies for public housing authorities at the level of at least $1.6 billion.

19. OPPOSE the demolition of public housing projects, unless the units are substandard and cannot be rehabilitated and the demolition is part of a comprehensive plan for housing which includes a feasible plan for relocation of all residents.

20. SUPPORT a three-year authorization of appropriations for operating subsidies.

21. SUPPORT the return of control of public housing operations to local housing authorities through deregulation.

22. SUPPORT provisions for incentives for better PHA management.

DISPOSITION

23. OPPOSE HUD's disposition of Secretary-held, assisted housing projects, unless adequate protection is provided to assure that the low-income character of the properties will be maintained, including, as necessary, a set-aside of Section 8 contract authority.

FHA/GNMA

24. SUPPORT FY 1983 commitment ceilings on the FHA mortgage insurance and the GNMA mortgage-backed securities programs at levels no less than FY 1982 ($40 billion and $68.25 billion, respectively).

25. SUPPORT continued funding of the GNMA Tandem programs in FY 1983 at amounts sufficient to meet the financing needs of projects to be developed.

26. SUPPORT realistic mortgage limits for all FHA programs.

27. SUPPORT the continuation of a comprehensive housing counselling program for FHA homeowners.

REHABILITATION

28. SUPPORT the authorization of new commitments under the Section 312 rehabilitation loan program out of repaid loan proceeds.

COOPERATIVE HOUSING

29. SUPPORT the conversion of assisted rental housing to cooperative ownership by low and moderate income families where displacement will not result.

30. SUPPORT an increase in the ceiling on the housing portion of the portfolio of the National Consumer Cooperative Bank to 50%.

MORTGAGE FINANCE

31. SUPPORT the extension of authorization for mortgage revenue bond financing for single-family housing beyond 1983.

32. SUPPORT amendments to the Mortgage Subsidy Revenue Bond Tax Act of 1980 to ease restrictions on multifamily and single-family mortgage bonds.

33. SUPPORT changes to pension fund legislation and regulations to facilitate investment in residential mortgages and to mandate that a reasonable percentage of pension fund assets be invested in residential mortgages.

34. SUPPORT the extension of the Credit Control Act and urge the President and the Federal Reserve Board, using the powers available under that Act, to allocate credit in a manner which directs more of the limited amount of credit toward the residential mortgage market at affordable rates.

35. OPPOSE the sale by FHA and GNMA of multifamily mortgages at deep discounts, to prevent the diversion of limited funds from new housing construction.

COMMUNITY DEVELOPMENT

36. SUPPORT FY 1983 funding of the community development block grant program at least at the level contained in the FY 1982 Appropriations Act ($3.456 billion).

37. SUPPORT appropriations for Urban Development Action Grants in FY 1983 of $645 million.

38. OPPOSE the inclusion of the community development block grant and urban development action grant programs, and other housing and community and economic development programs in the Administration's New Federalism proposal.

39. OPPOSE HUD regulations precluding use of UDAG funds for housing and neighborhood projects.

40. SUPPORT inclusion in any urban enterprise zone legislation of provisions which will encourage the construction and rehabilitation of housing, including units for low income families.

HUD OPERATIONS

41. SUPPORT sufficent appropriations for HUD staffing to permit it to handle adequately its workload during FY 1982 and FY 1983, including funds for the October, 1981 pay increases.

1982 Housing Crisis

The housing industry is in a crisis as a result of the continued tight money and budget slashing policies. The 1.1 million housing units started last year were fewer new housing units built than in any year since 1946. In each of the six months through January 1982, the annual starts rate was under 1 million. This has led to high unemployment in residential construction and related supplier industries. Both the housing industry and the economy at large have been hurt.

Sales of new and existing housing are down to low levels. Those who are able to buy homes are saddled with high debt burdens due to high interest rates. Meanwhile, federally subsidized housing production is being cut back in a move toward complete elimination.

Mortgage interest rates have risen steadily from an average of 9 percent in 1977. Major mortgage lenders charged an average effective rate of 16 percent at the end of last year for conventional home loans closed in the U.S., according to the Federal Home Loan Bank Board. For mortgages on which new financing commitments were issued, the average rate was 17½ percent.

Sales of new and existing homes were at a low level in December. New homes were sold at a seasonally adjusted annual rate of only 438,000. This rate was below the 1980 annual level and about 46 percent below the 1978 peak level of 817,000 sales for the year.

Existing home sales for December were also depressed at an annual rate of 1.95 million units -- down at about ½ the 1978 peak annual level of 3.8 million.

A shortfall of housing production relative to needs in recent years has created a serious, inflation generating shortage of housing.

There is a growing gap between the nation's housing needs and the supply to meet these needs. The Census Bureau projects an estimated annual net increase in households of about 1.75 million through 1985. In addition to units to accommodate the growth in households, there is a need for several hundred thousand additional starts each year to replace units lost from the supply due to demolition, fire, flood, and other catastrophies. As the population grows, more units are needed for vacancies to permit mobility and migration and to offset the absorption of units for second homes. There is a total annual need for approximately 2.4 million units before any allowance for additional replacement of occupied substandard units.

The consequences of underproduction are catching up with us in the high prices families pay for homes and apartments. In addition, there has been a reduction in available rental unit vacancies. Today, the rental vacancy rate is 5 percent, down from an equivalent rate of about 6.5 percent in 1973. The national rental vacancy rate among units with all plumbing facilities is only 4.5 percent. Many rental markets have became very tight. Thus, in the Northeast, the average rental vacancy rate is 3.7 percent, and it is lower in many localities. The rent index, which moves slowly, began to accelerate, rising by 6, 7, and 8.5 percent a year. When vacancy rates go down to low levels, prices shoot up and the mobility of people is inhibited.

During the seventies about 2.5 million rental units were created in single-family houses that became two-family structures, according to an estimate based on decennial Census figures. Such "undocumented conversions," often creating units by adding kitchens in basements and attics, were generally contrary to zoning and other local ordinances.

Older homes -- as well as some rental units -- have begun to house two or more families in a single unit. The doubling up of families, which had been declining since the immediate post-war years, reached a low of 1.3 million by 1974. By March 1981, the number of housing units with two or more families was over 1.6 million.

Subsidized housing waiting lists are growing longer as thousands of homeless "street people" seek adequate shelter in many cities, while federal housing budget cutbacks are reducing supply increases toward a zero level.

High mortgage interest rates threaten to continue the inadequate level of housing production into 1982 and beyond. Moreover, mortgage interest rates of 16 to 18 percent, as prevailed at the beginning of 1982, promise to make housing unaffordable to most prospective new home buyers and necessitate their resort to risky "creative financing" schemes in many instances in order to facilitate property conveyances even at high rates of interest.

The low level of housing production has also resulted in the idling of resources in building and related industries and high levels of construction unemployment. In February, the construction industry unemployment rate was 18.1 percent; and there were 928,000 unemployed construction workers.

In the face of a severely depressed housing industry and an economy falling into recession, the Administration is recommending a further retreat from federal involvement in housing and urban development.

For fiscal year 1983, the Administration is asking for an end to subsidized housing assistance for new and rehabilitated housing under the Section 8 and public housing programs, except for some housing for the elderly and handicapped under the Section 202 program. In contrast, Congress provided funds for fiscal 1982 which would produce an estimated 142,000 units of Section 8 and public housing at a mix of 45 percent new construction — substantial rehabilitation and 55 percent existing housing. However, even these funds were not secure, as the Administration is asking Congress to rescind previously approved funds for 59,000 units.

For fiscal year 1983, the Administration appears to favor a housing voucher program as the primary form of housing assistance. Housing vouchers would apparently be funded to aid about 215,000 families as a replacement for assistance currently received, including 191,000 units which would replace Section 8 existing housing certificates. Net additional families aided, therefore, would be only 24,000. This aid furthermore would not add directly to the supply of housing, but would increase the demand, aggravating inflationary pressures.

Needed housing starts would decline substantially under the Administration's 1983 budget for the U.S. Department of Housing and Urban Development (HUD).

To help revive the economy and reduce social hardships, the Congress must disapprove further cutbacks in assisted housing programs and act to provide adequate funding for low- and moderate-income housing programs.

SAVE-HOUSING COALITION

This is no time for complacency about housing in our country.

Young families, senior citizens, the poor, and even the not-so-poor are confronted every day with rising shelter costs and a growing housing shortage. Two families doubling up in houses built-for-one is no longer uncommon. Nor is the sight of homeless people sleeping in makeshift shelters. Those who build houses are being forced into bankruptcy and unemployment. Those who make the products out of which houses are built are idled. Those who manufacture the goods that make a house a home are seeing their markets vanish. Those who find and sell houses for people have few customers. Lenders who extend mortgage credit face an uncertain future. Those who govern our cities, towns and counties contend daily with housing and neighborhood deterioration that threatens the viability of their communiites. All of us are concerned that we will need shelter in the coming decade. Our existing housing stock will not last forever; it needs to be replaced, improved and rehabilitated.

We know that our Nation's resources are not unlimited. We know that we must take steps to expand our productive efforts. We know that the Nation today must make difficult choices about how we shall use our resources.

As representatives and leaders of national organizations concerned about the general welfare of our citizens and the future of our nation, we call upon the Congress and the Administration to "get down to basics." Shelter is basic. It is a basic human need that cannot long be ignored if life and community are to be sustained. Shelter is a basic industry. It provides productive employment for millions of workers directly -- and an even greater number in allied materials, equipment and furnishings manufacturing. We believe that housing needs should not be ignored -- and that building capacity should not be wasted.

We are deeply concerned by proposals to TERMINATE EXISTING COMMITMENTS for housing; RESCIND FUNDS which have already been appropriated; RAISE RENTS in LOW-INCOME housing; CURTAIL homeownership LOANS; CUT BACK on PUBLIC HOUSING and RENTAL ASSISTANCE; and ELIMINATE housing PRODUCTION and REHAB programs. Such proposals would adversely affect the elderly and handicapped, the rural poor and lower-income urban families -- groups who have already taken more than their share of budget cuts.

We believe this nation needs and can support housing programs that will provide adequate levels of production and assistance. We call upon the Congress and the Administration to preserve this nation's commitment to the goal of decent, affordable housing for all Americans.

Contact: National Housing Conference
223-4844

Contact: NATIONAL HOUSING CONFERENCE
(202)223-4844

SAVE HOUSING COALITION
(Participating groups)

AD HOC COALITION OF HOUSING FOR THE ELDERLY

AMERICAN FEDERATION OF LABOR/CONGRESS OF INDUSTRIAL ORGANIZATIONS
- AFL/CIO Housing Committee
- International Union of Bricklayers
- Brotherhood of Carpenters
- International Brotherhood of Electrical Workers
- International Union of Operating Engineers

AMERICAN ASSOCIATION OF HOMES FOR THE AGING

COMMITTEE AGAINST DISCRIMINATION IN HOUSING

COUNCIL OF STATE HOUSING AGENCIES

INTERRELIGIOUS COALITION FOR HOUSING

LEADERSHIP CONFERENCE ON CIVIL RIGHTS(Housing Task Force)

LEAGUE OF WOMEN VOTERS OF THE UNITED STATES

LUTHERAN HOUSING COALITION

MORTGAGE BANKERS OF AMERICA

NATIONAL ASSOCIATION OF COUNTIES

NATIONAL ASSOCIATION OF HOUSING & REDEVELOPMENT OFFICIALS

NATIONAL HOUSING CONFERENCE

NATIONAL LEAGUE OF CITIES

NATIONAL LEASED HOUSING ASSOCIATION

NATIONAL LOW-INCOME HOUSING COALITION

NATIONAL LUMBER AND BUILDING MATERIAL DEALERS ASSOCIATION

NATIONAL RURAL HOUSING COALITION
- Hispanic Housing Coalition
- Housing Assistance Council
- National Association of Farmworkers Organizations
- Rural America

NORTHEASTERN RETAIL LUMBERMAN'S ASSOCIATION

U. S. CONFERENCE OF MAYORS

Chairman GONZALEZ. Thank you, Mr. Weiner.
Mr. Helmbrecht.

STATMENT OF RICHARD K. HELMBRECHT, PRESIDENT, COUNCIL OF STATE HOUSING AGENCIES, ACCOMPANIED BY THOMAS W. WHITE, EXECUTIVE VICE PRESIDENT, AND GREGG SMITH, DIRECTOR, OREGON HOUSING DIVISION

Mr. HELMBRECHT. Mr. Chairman and members of the subcommittee, I am also the executive director of the Michigan State Housing Development Authority, in addition to serving as president of the Council of State Housing Agencies, whom I represent here today.

The Council of State Housing Agencies represents the 52 State authorized housing and finance agencies in 46 States, the city of New York, Washington, D.C., and the Commonwealth of Puerto Rico. With me today is Mr. Tom White, the executive vice president of the council and also Mr. Gregg Smith, administrator of the Oregon Housing Division.

Like the previous speaker, Mr. Weiner, I will stick to the text, but I don't think we need to elaborate much on the crisis that now confronts the housing industry. No single housing program will offer a complete response to the Nation's housing and economic problems.

The housing bill introduced by you, Mr. Chairman, and supported by many members of your subcommittee, looks to the future, but offers many of the components a strategy to preserve existing low-income rental units by carrying out housing production programs that have already been budgeted and appropriated.

From the viewpoint of the Council on State Housing Agencies, we see a number of key issues that could help alleviate the present housing crisis. First, preserving the existing low-income rental housing stock. Presently, the Nation is losing far more conventional rental units to demolition, abandonment, and condominium conversion than are being built. Increasing energy and maintenance costs for Government assisted housing seriously jeopardize the continued viability of these units. Rent increases for these low-income units will not be sufficient to offset operating cost increases.

Congress must take the necessary steps to insure that existing governmental assisted housing, the only affordable housing option for millions of low-income households, will be adequately maintained.

Second, build the units Congress already has budgeted and appropriated. Presently, there are as many as 110,000 units in the production pipeline. These are units for which funds have been appropriated by Congress but have not been built because of high interest rates. State housing finance agencies alone have as many as 35,000 section 8 units in the pipeline. Financing out of this pipeline will not only provide much needed low-income rental units now, but also provide an immediate shot in the arm for the residential construction industry but little or no additional budgetary impact.

I would emphasize that I commend, Mr. Chairman, one of the provisions of your bill which addresses the financial adjustment factor and would hopefully make it much more operable than it is right now.

Third, we do not believe bond-financed rental production can remain a possibility if the administration's industrial development bond proposal, which would prohibit accelerated appreciation of bond-financed rental units, is adopted. If this provision and additional restrictions proposed by the administration are adopted, rental housing bonds will be effectively terminated. Congress, following extensive study and debate, passed the Mortgage Subsidy Bond Tax Act of 1980. Although not perfect, this program hardly needs the additional restrictions on rental housing bonds now being proposed.

Fourth, Congress can make workable the $10 to $15 billion annual single family mortgage bond program they authorized in 1980. Because of the unworkable restrictions of the Mortgage Subsidy Bond Tax Act, less than $2 billion in single family bonds were sold under the provisions of that act last year. Congress should pass H.R. 4717, a bill which includes Senate amendments to the Mortgage Subsidy Bond Tax Act which should go to conference any day now.

However, for housing bonds to be self-supporting, it is critical that allowable yield for revenue bonds be raised to 1.25 percent. With this arbitrage level, and with a leveling off of interest rates, we anticipate that $10 billion in housing bonds could be sold this year. This volume of housing bonds would directly finance 180,000 moderately priced housing units at below market rates. This volume of housing bonds would create 330,000 jobs in construction and related employment areas, and generate $1.8 billion in State, local, and Federal taxes.

Housing bonds are not a panacea for the housing industry, but there is no question that a workable bond program could be implemented immediately. A delivery system is in place. The costs to the Federal Government have already been budgeted.

Fifth, we encourage Congress to seek new options and partnerships in the production of much needed low- and moderate-income housing. With modifications, the Council on State Housing Agencies supports the rental production program included in this proposed legislation. The program's reliance on State and local administration and flexibility are definite improvements over past Federal rental housing production programs.

The Council of State Housing Agencies' specific modifications for this program include: One, Federal project approval under the rental production program shall not be done on a project-by-project basis. The council suggests a set-aside for States and large urban areas. Two, allocation of program funds should follow a Federal equitably established formula to assure adequate funding for rural areas and to meet the special housing needs of the elderly and handicapped. Three, a workable FHA support program such as coinsurance should be developed. Four, a clear role for tax-exempt financing must be included in the program design to maximize the leverage of State and local participants. Five, for social and economic reasons, Congress should consider and resist efforts to make the rental program totally low income or to provide incentives for 100 percent low-income projects.

With the modifications noted above, the proposed production program could effectively stimulate the production of low- and moderate-income rental housing and be adaptable to the special housing needs of the rural areas, the elderly, and the handicapped.

The crisis in low- and moderate-income housing requires strong action by Congress not only to meet pressing economic and housing needs, but to put in place a system that will address these needs for years. H.R. 5731 goes a long way in this direction by preserving the existing stock of low-income units, allowing for use of section 8 funds that have already been budgeted and appropriated, and by anticipating low- and moderate-income housing needs.

The Council on State Housing Agencies looks forward to working with you, Mr. Chairman, and members of the subcommittee, in this critical legislation. Again, I thank you for the opportunity to testify.

[Mr. Helmbrecht's prepared statement, on behalf of the Council of State Housing Agencies, follows:]

Prepared Statement of

Richard K. Helmbrecht
President, Council of State Housing Agencies
Before the
U. S. House of Representatives
Subcommittee on Housing and Community Development

March 23, 1982

Mr. Chairman and members of the Housing and Community Development Subcommittee, thank you very much for the opportunity to testify today. My name is Richard K. Helmbrecht and I am Executive Director of the Michigan State Housing Development Authority. I also serve as President of the Council of State Housing Agencies. The Council of State Housing Agencies represents the 52 state-authorized housing finance agencies in 46 states, the City of New York, Washington, D.C., and the Commonwealth of Puerto Rico. Included in our membership are participants in the state housing finance industry including investment bankers, builders, developers and non-profit organizations.

Overview of Key Issues

The Housing Slump Is In Its Third Year

The downturn in housing production which began in the late summer of 1979 has grown worse over the passing months. With housing production at post-war lows and over one million construction industry workers unemployed, there can be no doubt that we have a depression in the housing industry. A shutdown of the housing industry has widespread impact on the economy. Revenues from property tax, home sales and related retail sales taxes, income and corporate tax and other fees associated with the sale of new and existing homes have fallen substantially. In place of these revenues to local, state and federal government we have rising unemployment, welfare claims and builder bankruptcies. Many sectors of the U.S. economy are suffering during the present rescession. None have borne the burden of high interest rates more heavily than the construction industry.

Conservative estimates of household formation, losses to the existing stock and necessary vacancy allowances indicate that we will need about 2.45 million new housing units per year during the decade of the eighties to maintain present levels of housing quality and availability.1/ If present trends persist, we are unlikely to have annual production this year that is much higher than last year's dismal level of 1.08 million starts.

The implications of this production shortfall are clear. Across income levels, renters and first-time home buyers will face a rapidly falling standard of living as prices for housing units will be bid up — where units are available. Most people who presently own homes will be in good shape if they aren't required to move and if their housing needs don't change.

The housing prospects for households at the lower end of the income scale are becoming grim. Rental shortages are forcing middle income households to compete directly with lower income renters for units. The vacancy rates for units affordable to moderate and low income households are significantly below the national vacancy rate for all rental units. Although public housing and Section 8 projects provide decent and affordable housing for millions of low income households, waiting lists for these units are long. For example, 40,000 Baltimore families are waiting for a vacancy in one of the city's 18,000 public housing units. New applicants for Dade County, Florida low income units face a 20-year wait.[2]

H.R. 5731, the House housing authorization bill, plays a very important role in addition to its traditional role of affirming the nation's commitment to a decent home for every American household. This bill has a critical function as an economic stimulus package whose benefits will spill over from the construction industry to many other sectors of the U.S. economy.

A Housing Policy Perspective

No single program will provide an effective response to the nation's housing and economic problems. The housing bill introduced by the Chairman and many of his colleagues on the subcommittee, offers many of the components of a strategy to preserve existing low income rental units, carry out housing production programs that already have been budgeted and appropriated, ensure a smooth transition from existing production programs and create new rental production programs that are appropriate for the eighties. In the following sections, I will outline some of the key issues relating to this comprehensive response to this nation's housing and economic plight.

Preserve the Existing Low Income Rental Housing Stock. Presently, the nation is losing far more conventional rental units to demolition, abandonment and condominium conversion than are being built. Increasing energy and maintenance costs for the government-assisted housing stock seriously jeopardize the continued viability of these units. Rent increases for these low income units will not be sufficient to offset these operating cost increases. For both conventional and government-assisted units, the cost of replacing these units will be prohibitive. Congress must take the necessary steps to ensure that existing government-assisted housing, the only affordable housing option for millions of low income households, will be adequately maintained.

To preserve the existing stock of government-assisted low-income housing, Congress must ensure that the annual adjustment factors used by HUD to assign Fair Market Rents (FMRs) on government-assisted housing appropriately reflect the true operating cost increases faced by these projects. Similarly, cost amendments to rental assistance contracts must appropriately parallel these FMR increases to keep government-assisted units affordable for low income households. Although default rates on HFA-financed rental housing have been shown to be among the lowest for government-assisted housing, CSHA supports the continued funding of the flexible subsidies program as a necessary and efficient means to place marginal projects back on a stable financial base.

Build the Units Congress Already Has Budgeted and Appropriated. Presently, there are as many as 110,000 units in the production pipeline. These are units that have been appropriated by Congress but have not been built because of high interest rates. State HFAs alone have as many as 34,000 Section 8 units in the pipeline. The appropriated units in the pipeline constitute a full year's low income housing production. Financing out the pipeline not only will provide much-needed low-cost rental units but will also provide the most immediate "shot in the arm" for the residential construction industry with little or no additional budgetary impact. Although State Agencies projects are not eligible for such financing, CSHA supports the measure in H.R. 5731 which will provide GNMA tandem financing. To get the pipeline going and as included in H.R. 5731, Congress also must raise the financing adjustment factor (FAF) for bond-financed projects to reflect market interest rates and the construction start deadline for FAF eligibility must be extended from June 1st. Finally, non-FAF amendments must not be arbitrarily capped. Without additional higher amendment authorization, many projects won't be workable even under a FAF which recognizes market rates.

To Keep Bond-Financed Rental Production a Possibility, Congress Must Reject the Administration's Industrial Development Bond Proposal Which Would Prohibit Accelerated Depreciation of Bond-Financed Rental Units. Because of this provision and additional restrictions proposed by the Administration, rental housing bonds will be effectively terminated. Congress, following extensive study and debate, passed the Mortgage Subsidy Bond Tax Act. Sixteen months later, the Administration is proposing additional restrictions on rental housing bonds. These restrictions must be rejected (please see attachment #1).

Congress Must Make Workable the $10 To $15 Billion Annual Single Family Mortgage Bond Program They Authorized In 1980. Because of unworkable restrictions in the Mortgage Subsidy Bond Tax Act, less than $2 billion in single family bonds were sold under the provisions of the Act last year. Congress should pass H.R. 4717, a bill that should go to conference any day now, which includes amendments to the Mortgage Subsidy Bond Tax Act. However, for housing bonds to be self-supporting, it is critical that allowable yield for revenue bonds be raised to 1.25%. With this arbitrage level, we anticipate that $10 billion in housing bonds will be sold this year. This volume of housing bonds would directly finance 185,000 moderately priced homes at below-market rates. This volume of housing bonds would create 330,000 man-years of housing construction-related employment and generate $1.8 billion in local, state and federal taxes. Housing bonds are not a panacea for the housing industry, but there is no question that a workable bond program could be quickly implemented. The costs to the Federal government have already been accounted for (please see attachment #2).

Seek new options and partnerships in the production of much-needed low and moderate income housing. With modification, CSHA supports the rental production program included in H.R. 5731. The program's reliance on state and local administration and the flexibility of the program are definite improvements over past federal rental housing production programs. In addition, the recognition of the value of mixed-income projects is an important aspect of this program. CSHA recommends, however, that funding not be done on a project-by-project basis. A federal fair share approach would ensure the allocation of funds to rural and other underserved areas. Effective support programs, such as co-insurance would add to the workability of the program. It must be made clear that the program is compatible with tax exempt financing to ensure that state and local government will be able to leverage limited federal dollars. With the modifications noted above, the proposed production program could efficiently stimulate the production of low and moderate income rental housing and be adaptable to the special housing needs of rural households, the elderly and handicapped individuals.

The crisis in low and moderate income housing requires strong action by Congress, not only to meet pressing immediate economic and housing needs, but to put in place a system that will address these needs for years to come. H.R. 5731 goes a long way toward preserving the existing stock of low income units, allowing for use of program funds that have already been budgeted and appropriated, ensuring an orderly transition to new programs and setting in place new programs which will effectively and efficiently meet low and moderate income housing needs for years to come. I would now like to discuss in more detail some of the provisions of H.R. 5731 and a number of related issues.

Preservation of the Existing Low and Moderate Income Housing Stock

Over the period of the last twenty years, the Federal government has provided housing for millions of Americans, many of whom to this day remain in government assisted housing. Young couples, large families, the elderly and handicapped of all races and pursuasions are assisted through government housing. The Federal Government must not abandon millions of people sheltered in government assisted housing. Adequate solutions must be arrrived at which reflect both a cost effective yet compassionate approach to support government assisted housing so that it can remain available to those who need it. The issues encountered today with respect to government assisted housing can be understood in a broad sense in terms of:

- operating costs which have risen over time and programs which do not accurately reflect the cost increases; and
- stagnant tenant incomes which can not support necessary rent increases.

To insure that present assisted housing is maintained and that rents continue to be affordable for the occupants, we strongly encourage Congress to maintain adequate levels of Public Housing Operating Subsidies.

In addition, the many Section 236 rental projects that rely on federal interest payments require Congressional attention. Special deep subsidies allow many 236 occupants to pay a fixed percentage of income toward rent. Without amendments to increase the money available to the projects, these low income families will not be able to stay in their homes. Congress and the Administration are aware of these needs and are taking steps to fund the rent supplement program which provides assistance for the majority of these families. However, we are seriously troubled by a management process which has left unfunded the increases needed for 1981, and a process which is replacing rent supplement in FHA projects with Section 8 but which has thus far ignored state non-insured projects.

Funding must continue to be equitably provided to support both state agency insured and non-insured projects. Limited funding available as proposed for two years will place State Agency projects currently assisted under rent supplement at risk - threatening the continued occupancy of such units by low and moderate income persons.

CSHA will be providing staff a detailed analysis of this issue. We stress, however, the need for Congress to insure continuity in the present program and equity to non-insured project occupants.

Section 8 Existing and Housing Vouchers Programs

The Council of State Housing Agencies was pleased to see the Committee maintain the current Section 8 Existing program criteria. Although the details of the Administration's proposal have not yet been made available, CSHA is concerned that the Administration will attempt to replace the current Section 8 Existing program with a less effective voucher program. Sixteen state housing finance agencies and a number of state community development agencies currently adminster the Section 8 Existing program and believe it to be a highly successful program.

Design features of the current Section 8 Existing program which we feel are particularly worth maintaining include:

1.) monthly payment should go directly to the landlord to ensure their participation in the programs and avoid potential abuses.

2.) subsidy should continue to be in the form of a standard payment based on housing costs (like Fair Market Rents), rather than a percentage of income. The Fair Market Rent system was established precisely for the purpose of reflecting real housing costs and CSHA believes the system is working rather well.

3.) Minimal Housing Quality Standards must be retained nationwide with some allowance for regional variation. Without housing quality standards this program would be indistinct from an income maintenance program. Continuing these minimum quality standards guarantee that the program meets its purpose of improving the living conditions of low income households.

4.) Although the current state/local negotiated administration system is working, real efficiencies are gained through state administration. Central administration results in consistent interpretation of guidelines and uniform operations. A single administering entity can enforce more controls against fraudulent use of the housing payments. Significant economies of scale can be obtained through state-wide operation, as administrative overhead costs are spread more thinly. State housing or community development agencies are in an ideal position to oversee housing quality standards throughout the state. The state can fill the gap for the many rural localities which have no housing codes and cities without the capacity to conduct housing inspections. Participants are guaranteed greater housing choice and mobility as the administering jurisdiction increases in size.

Funding the Pipeline

Estimates of the total number of units which could be provided for low and moderate income occupancy, which are today lodged in both the HUD and the state agency Section 8 pipeline, are placed at well over 100,000 units. Immediate action can be taken by the Congress and the Administration to alleviate the pressing demand for new rental housing, action which would create thousands of new job opportunities in today's all but crippled housing industry.

The Congress and the Administration are to be congratulated for their actions last fall establishing a Financing Adjustment Factor (FAF).

Representative Gonzalez and the sponsors of HR 5731 are to be commended for recommending statutory changes to the FAF. The FAF was designed to enable projects to be processed taking into account unusually high interest rates. Section 8 Fair Market Rents are adjusted in accordance with the terms of the permanent financing with a maximum of 12%. However, even with the FAF, projects continue to be infeasible. Presently at issue is the fact that the 12% interest rate ceiling mandated by the FAF regulations does not accurately reflect current interest rates.In addition, the FAF regulations mandate that construction on all FAF projects must commence by June 1, 1982. Market conditions simply will not allow for this schedule to be held. Congress can take immediate steps to make the FAF workable by:

- permitting the 12% interest rate ceiling currently mandated by the FAF regulations to be raised to more accurately reflect current interest rates; and
- extending the date by which construction must commence on all FAF jobs from the current June 1 start date.

CSHA urges Congress to re-evaluate the current recapture/reuse ceiling specifically applicable to the FAF (now set at 1.4 billion dollars nationwide) to determine whether this cap on reuse of previously commited Section 8 authority would artificially inhibit the development of Section 8 pipeline projects.

Two other barriers to project financing have been created by OMB. They have influenced HUD to revise the manner in which state agency units are transferred, and for all projects they have changed non-financial amendment policies without a change in regulation. These changes may preclude financing the pipeline, however, they are very technical in nature. We know committee staff have been instructed to review the issues involved and we will work with them and with HUD to seek early resolutions so we can get on with building low income projects which will reemploy thousands of workers.

Developing New Production Alternatives

Losses to the existing rental housing stock, the lack of low and moderate cost housing construction and rental demand pressure created from households unable to afford ownership units, all set the stage for a low and moderate cost rental supply crisis in the eighties.

Since the middle seventies, the economics of rental housing production have made rental housing production nearly impossible without below market financing and governmental assistance. Despite the fact that half of the rental households in the country earn less than $10,000 per year, in 1980 only 6,100 unsubsidized rental units with rents below $200 per month were completed.

In the eighties we must continue govermental assistance to rental housing. The sponsors of HR 5731 are to be congratulated for recognizing the need for such assistance while striving to achieve significant cost savings over prior programs. The Council will be submitting additional comment on the rental production program envisioned in HR 5731. In this testimony we will focus on the broad provisions of the program.

We generally support the program envisioned as we support greater reliance on state and local housing program administration. The success of state finance agency housing programs in the 70's, and the success of local community development efforts, all point to the fact that non-federal program administration is effective.

In view of a decreased dollar commitment to housing, we support the flexibility the suggested program would give to participants. In these days of tight budgets, maximum opportunity to leverage funds is critical and the proposal will allow for this.

We suggest that further clarification of the federal role in project selection is necessary. As presently written, the program seems to contemplate federal selection on a project-by-project basis. We understand there may be need for project approval similar to Section 8 program, however, we suggest use of the following concepts in deciding how the program would be administered:

- A setaside for states and large cities;
- Use of Certifications rather than HUD approvals;
- Use of a Post Audit System for enforcement; and
- Clear reliance on State and local processing.

This will promote the development and continuation of professional state and local housing staff.

To ensure reasonable and consistent access by developers, requirements for open project selection should be required of the state and local participants.

The HUD focus should be on establishment of support programs for the state and local effort. An example of this would be the development of an effective co-insurance program, or perhaps a housing program as submitted to this committee by the Ad Hoc No Name Coalition and contained in the National Leased Housing Association testimony.

We support the mixed income concept in the legislation. We urge the committee to resist any efforts to make the program totally low income or to provide incentives for 100% low income projects. This program will be the only production program available. If all resources must be directed to low income occupants, the nature of the effort would shift to income transfer away from its present focus on housing stock.

We urge the Committee to reject any efforts to limit the program to rehab or to low income areas as apparently the Administration will advocate when they introduce their housing proposals.

It must be made clear that tax exempt financing is a part of the concept. Without such financing, state and local government will be hamstrung.

We favor a federal fair share. The fair share should:

- Ensure program availability in rural areas;
- Allow for use of funds to meet special housing needs such as elderly housing; and
- Set aside a block of funds for proven housing agencies such as state finance agencies.

We would stress the elderly housing potential in this program. Elderly housing has much to recommend it. The growth in the elderly population will continue at least until the year 2020. Long term commitments to elderly housing stock are thus demographically sound as money spent for decent facilities will have a long useful life. The construction of mixed income, congregate service facilities makes good public policy:

- Elderly housing is popular with the occupants;
- Such housing frees up under-utilized family homes; and
- Hospital and medical care costs can be saved.

In summary, this committee should encourage state government to make special efforts to develop cost effective elderly housing programs by leveraging funds such as in this proposal.

State Finance Agencies will be making a special effort to develop creative suggestions for your consideration. We will work with your staff to help them any way we can. Again, we believe your proposal will mark a historic new beginning for housing as it envisions the reality of a new federalism based on state, local, and federal partnerships with private enterprise.

Summary Recommendations to Congress

The housing legislation introduced by Congressman Gonzalez and his colleagues provides an effective stimulus for the housing industry and maintains the federal government's commitment to improve housing opportunities for low and moderate income households. In the coming weeks, the Council of State Housing Agencies welcomes the opportunity to work with Congress to further refine the provisions of H.R. 5731 to ensure that the legislation offers the most immediate relief for the depression in the housing industry and provides the most efficient delivery of housing services to low and moderate income households. CSHA strongly supports the general intent and major provisions of H.R. 5731. To improve the impact and efficiency of the bill, CSHA offers the following recommendations to Congress.

Preservation of the Existing Low and Moderate Income Assisted Housing Stock

- HUD Fair Market Rents must accurately reflect the true cost of operating and maintaining existing low income housing projects. Rental assistance payment contracts must reflect these costs and not place an unreasonable burden on low income households.
- Congress must ensure that non insured state financed projects which require rent supplement and rental assistance payment (RAP) are provided a level of funding authority and a distribution policy which adequately recognizes needs existing outside of the HUD insured portfolio.
- The Flexible Subsidies Program, an efficient means to restore troubled low income housing projects to a stable financial base, must be continued.
- The Section 8 Existing Program, a proven means to promote the preservation and moderate rehabilitation of the existing stock, must be continued. Housing vouchers are not a substitute for this program.

Financing the Section 8 Pipeline

- The current FAF interest rate ceiling of 12% should be raised to more accurately reflect current market interest rates.
- Extend the date by which construction must commence on all FAF projects from the current June 1 start date.
- The current recapture/reuse ceiling specifically applied to the FAF (now set at 1.4 billion) should be re-evaluated relative to the number of projects to be processed under the FAF guidelines.

- Amendment policies recently imposed by HUD outside the normal regulatory process should be withdrawn. Effective cost containment measures already exist in the Section 8 regulation in addition to voluntary cost containment measures underway in most state agencies.

- The Administration's policy decisions regarding the transfer of Section 8 and other funds previously applied to state housing finance agencies should be withdrawn to enable state agencies to effectively finance the pipeline.

Pass Legislation to Make Housing Bonds a Workable Housing industry Stimulus and Means for Providing Affordable Mortgage Capital

- Congress should act quickly to pass Senate amendments to H.R. 4717. These amendments include protections against reserve fund losses and increase the 20% low income requirement for multifamily projects to 80% of median income for 10 years. Arbitrage provisions should be increased to 1.25%.

- Congress should push the Administration to issue workable multifamily regulations, and to revise the present unworkable single family regulations.

- Congress should reject efforts by the Administration to increase restrictions on multifamily housing as a part of Industrial Development Bond legislation.

- Congress should pass legislation eliminating the 1984 sunset provision for single family bonds.

Develop Effective Low and Moderate Income Housing Production Programs

- Project approval under the rental housing production program included in H.R. 5731 should not be done on a project by project basis. CSHA suggests a setaside for states and large urban areas; the use of certifications rather then HUD approvals; the use of post audits for enforcement; and a clear reliance on state and local processing.

- Allocation of program funds should follow a federal fair share approach to ensure adequate funding for rural areas and meet the special housing needs of the elderly and handicapped.

- Workable FHA support programs such as co-insurance should be developed.

- A clear role for the tax-exempt financing must be included in the program designs to maximize the leverage of state and local participants.

- Congress should resist efforts to make the program totally low income or to provide incentives for total low income projects.

This concludes my prepared remarks. As noted earlier, CSHA is now preparing a more detailed analysis of the proposed rental housing, production program. This analysis will be delivered to the subcommittee very soon. CSHA looks forward to working with the Chairman in every capacity on this critically important legislative package. I would be happy to answer questions at this time.

1/ ICF Incorporated. Housing Needs In the 80's. Washington, D.C., February 1981.

2/ "Public Housing Agencies Face Cuts As Demand, Repair Costs Mount" Daily Bond Buyer. March 19, 1982 : 19.

ATTACHMENT #1

COUNCIL OF STATE HOUSING AGENCIES

Administration Proposed IDB Legislation Will End Low and Moderate Income Rental Housing Bonds

The Administration's proposed legislation to curb the sale of industrial development bonds not only applies to rental housing bonds used by state and local government to finance the production of critically-needed low and moderate income rental housing, if passed, the legislation will effectively end this program. The combination of these proposed restrictions with the restrictions already set in place under the Mortgage Subsidy Bond Tax Act of 1980 will make issuance of rental housing bonds a virtual impossibility. In a separate proposal, the Administration also will nearly eliminate the Section 8 and public housing production programs. The Administration IDB proposal will remove from the hands of state and local government their most effective means for shouldering the responsibility of moderate income rental housing production.

The economics of rental housing production, as demonstrated since the mid-seventies, have made moderate income rental housing production nearly impossible without below market financing and preferential tax treatment. Despite the fact that half of the renter households in this country earn less than $10,000 per year, in 1980 only 6,100 unsubsidized rental units with rents below $200 per month were completed. Last year in recognition of the need to stimulate rental housing production, the Congress passed legislation to improve the tax treatment of rental housing. Under the Administration IDB proposal, prohibiting the application of the Accelerated Cost Recovery System (ACRS) to bond-financed rental projects, will require that rents must rise as much as $200 per month to offset the loss of the tax benefit. With the present low income requirement for bond-financed rental housing, eliminating accelerated depreciation will make these projects economically infeasible or unaffordable by low income tenants. Either way, bond-financed rental housing won't be built.

Rental Housing Bonds Received Extensive Congressional Scrutiny and Targeting Restrictions In the Mortgage Subsidy Bond Tax Act of 1980.

Following two years of study and debate, Congress passed the Mortgage Subsidy Bond Tax Act of 1980. As an outcome of that law, all rental housing bonds issued since January 1, 1982 must be in registered form (a provision also included in the Administration proposal). The 1980 Act also stipulates that, in bond-financed rental projects, at least 20% of the units must be reserved for low income households (a more specific targeting provision than what is included in the Administration proposal).

In recognition of the critical public purpose played by multifamily bonds, Congress exempted them from the 1984 sunset that was applied to single family bonds. Moreover, because of the costs and risks associated with low and moderate income rental housing development, Congress exempted multifamily bonds from the strict arbitrage and reserve fund restrictions that were applied to single family issues.

The key point is that, sixteen months ago, Congress completed lengthy deliberations on housing bonds and produced legislation to ensure their targeted and

1133 15th STREET, NORTHWEST / SUITE 514 / WASHINGTON, D.C. 20005 / PHONE: (202) 659-6560

efficient use. There have been major problems with the Mortgage Subsidy Bond Tax Act, not the least of which is the virtual preclusion of self-supporting single family bond sales. Rather than starting from scratch on an entirely new piece of housing bond legislation, CSHA strongly recommends that Congress make the needed "fine-tuning" adjustments to the 1980 Act and exclude rental housing bonds from the Administration proposal.

Rental Housing Bonds Are Not a Run-Away Program

There is a significant error in the Adminstration's explanation of its IDB proposal ("General and Technical Explanations of Tax Revisions and Improved Collection and Enforcement Proposals, " Department of the Treasury, February 26, 1982). On page 25, the Administration charts the growth of "Housing" bonds between 1976 and 1981. Although the proposal does not apply to single family mortgage revenue bonds, single family bonds were included in the annual totals. Below, Table 1 accurately compares annual volume of rental housing bonds and small issue IDBs since 1976. Average annual growth of rental housing bonds over the last five years has been less than 11%. In fact, rental bond volume has been dropping steadily since 1979. These annual totals closely follow production levels under the Section 8 program. Fully one-third of all Section 8 units have been financed by state housing finance agencies with bonds. Combining state HFA and local bond financing via the 11-b program accounts for the vast majority of multifamily rental housing bond issues during the last six years. If the purpose of the Administration proposal is to curb runaway growth in IDB volume, such measures are unnecessary for rental housing bonds because market forces relating to rental housing development and cut backs in federal production assistance programs already serve that purpose.

The Nation Faces a Major Crisis In Rental Housing Supply

Eliminating federal supports for low and moderate income housing production and severely restricting state and local access to tax exempt rental housing bonds will cut national rental housing production in half and virtually eliminate all low and moderate income rental housing production.

The reason unsubsidized rental housing is not being built in any quantity is that households who can afford the rents required by new rental units more often than not can afford to buy a home. As a result, homeownership has "creamed off" the higher income renters and left a renter population unable to afford newly built units. Beside the fact that few non-luxury conventional apartments are being built, annual losses to the rental stock due to condominium conversion, abandonment and demolition are having a devastating effect on rental housing supply. George Sternlieb of Rutgers University

---

Table 1

Small Issue IDB and Rental Housing Bond Growth 1976-1981*

	1981	1980	1979	1978	1977	1976
Small Issue IDBs	10.5	8.4	7.1	3.5	2.3	1.5
Rental Housing Bonds	3.7	4.1	5.6	3.7	2.3	2.4

---

*Statistics from Daily Bond Buyer and Congressional Budget Office estimates that demolition and abandonment losses to the existing rental stock will average 578,000 units annually during the eighties.

Estimates of increases in rental need resulting from household formation range from 290,000 to 400,000 units per year throughout the eighties. When losses to the existing stock are added to household-formation-related statistics we see—as a minimum—that an annual rental production requirement of 600,000 units per year is needed to maintain the current rental supply. Advance Mortgage Corporation reports that in 1981, conventional unsubsidized apartment starts were slightly over 100,000 units—at all price ranges. With the federal government backing out of low income rental housing production and if these proposals to strangle rental housing bonds are passed, how will the critical need for low and moderate income rental housing production be met?

The Administration Offers No Low and Moderate Income Rental Housing Production Alternative to Rental Housing Bond Programs

The Administration proposes to terminate all federal assistance for the production of new and substantially rehabilitated Section 8 housing and public housing. The total commitment of the federal government to low cost rental housing production is 10,000 units of Section 202 elderly housing under the Administration's 1983 proposal. The Administration also is seeking to cancel tens of thousands of Section 8 units that were appropriated in prior years and now are in the production pipeline.

The Administration offers a housing voucher program as its response to the plight of low income rental households across the country. The Experimental Housing Allowance Program demonstrated clearly that housing vouchers will do little to promote moderate rehabilitation of rental housing and nothing to promote new construction or substantial rehabilitation. Nothing. As the number of rental units declines due to abandonment, demolition and condominium conversion, housing vouchers will simply provide more dollars to chase after a steadily declining number of goods.

Because of the high cost of rental housing production, rental housing bonds alone cannot replace Section 8 and public housing as a direct response to the housing needs of low income renters. Rental housing bonds do offer state and local government a practical means to continue to produce moderate cost rental housing. Applying housing vouchers to bond-financed rental units will make workable the low income requirements for bond-financed projects. State housing finance agencies alone have financed 360,000 low and moderate income rental units with bonds. By restricting state and local access to rental housing bonds, the federal government will dismantle state and local low and moderate income housing delivery systems while, at the same time, they are dismantling HUD and FmHA low income rental housing production assistance capacity.

The Administration Proposal

The Administration proposal to restrict IDBs has four major provisions that will directly impact on rental housing bonds:

- All rental housing bond issues are to be subject to public review and approval by elected representatives of state or local government;
- After 1985, state or local government must provide for the rental development an in-kind contribution with a present value equal to 1% of the bond issue;

- Rental housing developments financed with tax exempt bonds cannot benefit from the depreciation provisions in the Accelerated Cost Recovery System implemented under the Economic Recovery Tax Act of 1981; and

- Agencies will not be allowed to earn arbitrage on the interim investment of bond proceeds or on the investment of reserve fund capital. Bond underwriter discounts and bond counsel fees cannot be applied to calculations for arbitrage limitation purposes.

All of these proposals significantly increase the degree of federal regulation over rental housing bond issues. The public review requirement will jeopardize the timing of bond sales and may allow small community factions to delay project construction due to objections over project siting. Presently, all state HFA bond issues are subject to review and approval by boards appointed by state governors and legislatures.

Requiring an in-kind contribution from state government may be workable in some cases. However, a provision of this kind clearly discriminates against less affluent states—the very same states that may be most in need of low and moderate income rental housing.

Excluding bond-financed rental housing from the accelerated depreciation provisions of the Economic Recovery Tax Act will effectively restrict low and moderate income rental housing investment to a small number of nonprofit corporations. Investor owners will not build low and moderate income rental housing because the opportunities for appreciation will, in most cases, not offset the costs and risks. Rental housing investment syndicates will be ruled out entirely. Many non-profit groups rely on the syndication process to raise capital for housing services, reserve funds and to lower rents. More than any other provision of the Administration proposal, the exclusion of bond-financed properties from accelerated depreciation will kill investment in low and moderate income rental housing.

The arbitrage and reserve fund sections of the proposal involve another attempt to weaken the security of low and moderate income rental projects. A similar proposal was rejected by Congress in the Mortgage Subsidy Bond Tax Act. If passed into law, these restrictions would eliminate the ability of issuing agencies to develop the cash reserves necessary to ensure the long-term viability of rental projects.

These measures, in tandem with the restrictions already implemented under the Mortgage Subsidy Bond Tax Act, will make it extremely difficult for state and local government to issue rental housing bonds. Where bond issues are workable, the prohibition regarding accelerated depreciation will preclude any private investment in low and moderate income rental housing.

Conclusion

Congress, following lengthy examination of the issue, recently passed comprehensive housing bond legislation in the Mortgage Subsidy Bond Tax Act. The shock waves that the 1980 Act sent through state and local government are still being felt. The Senate recently has passed legislation to remove a number of the most impractical aspects of the 1980 Act. Taking up new, and far more restrictive, housing bond legislation is premature and clearly unjustified given the great need for rental housing and the declining role of the federal government in low and moderate income rental housing production. The Council of State Housing Agencies strongly recommends that Congress strike all reference to rental housing bonds in this legislative proposal.

ATTACHMENT #2

COUNCIL OF STATE HOUSING AGENCIES

In Support of Mortgage Revenue Bonds

In 1980, Congress perceived a danger in unlimited mortgage revenue bond (MRB) programs and passed legislation to limit bond volume and target the use of bond proceeds. Unfortunately, technical provisions of the law, unrelated to the targeting and volume restrictions, have made MRB programs virtually unworkable. Despite regulatory action by the U.S. Treasury to relax some of the restrictions, 1981 MRB issues covered by the 1980 Act amounted to less than $2 billion: less than 15% of the Congresionally-imposed volume limit. The majority of these issues required a contribution from HFA reserves or state appropriations to cover issuance cost shortfalls resulting from restrictions on the use of bond proceeds.

The Need for Mortgage Revenue Bonds

- Despite unprecedented housing needs, single and multifamily housing production is at its lowest post-war level. Conservative projections of interest rate levels for 1982 suggest that the depression in housing, now in its third year, will continue.
- Unemployment in the housing and real estate industries now numbers over one million. The lack of affordable mortgage capital jeopardizes the viability of all sectors of the housing industry and sets the stage for large scale housing-related price inflation when the economy does recover.
- Losses to the existing rental housing stock, the lack of low and moderate cost rental housing construction, and rental demand pressure created from households unable to afford ownership units all set the stage for a low and moderate cost rental supply crisis in the eighties. Presently, we are losing more units than we build.
- Low income families need low cost energy and home improvement loans. Only tax exempt financing can provide these loans at reasonable interest rates. Otherwise the retail rates, which are well above mortgage rates, must be paid.

The Benefits of Mortgage Revenue Bonds

- To date, State HFAs have used mortgage revenue bonds to finance 418,000 single family and 360,000 apartment units. No two HFAs are alike in the way that they have tailored their programs to serve state housing needs.
- $1 billion in mortgage revenue bonds will provide direct below-market financing for 18,500 first-time homebuyers. The direct and induced sales effect of $1 billion in MRBs totals over 40,000 housing units.

- $1 billion in mortgage revenue bonds will stimulate the production of 15,000 new homes. This housing production will provide 33,000 man-years of construction-related employment.

- In the first year, $1 billion in revenue bonds will generate $126 million in federal personal and corporate income taxes and $54 million in state and local tax revenue. Annual real estate taxes alone on 15,000 new bond-financed units ($18.56 million) will nearly offset federal revenue expenditures associated with $1 billion in bonds. In sum, mortgage revenue bonds are a net generator of tax revenue for federal, state and local government.

- The social benefits of mortgage revenue bonds include making the dream of ownership a reality for thousands of renters. By freeing up rental units, pressure in the rental market is reduced. Bond capital is the only affordable source of home improvement and energy conservation retrofit capital for thousands of American households. Bond programs allow state and local government to take responsibility for housing and promotes the elimination of ineffective federal bureaucracies.

The Costs of Mortgage Revenue Bonds

- Estimates of the annual revenue expenditures of mortgage revenue bonds range widely. The Congressional Budget Office estimate, $22.5 million per $1 billion in bonds, falls in the mid-range of these estimates. This estimate, however, does not take into account the reduction in the maximum tax rate on unearned income from 70 to 50 percent.

- Arguments that MRB programs will deluge the municipal bond market and spur significant increases in bond yields are no longer valid given the housing bond volume limitations imposed by Congress.

- Presently, 75% of all tax expenditures for housing accrue to households earning more than $30,000 per year and claiming mortgage interest and property tax deductions ($30 billion per year according to CBO). CBO estimates that mortgage revenue bonds account for less than 5% of all housing-related tax expenditures.

- During a time when nominal declines in housing prices are being seen across the country, MRB programs are not likely to have an inflationary impact on housing prices. In fact, by preventing the collapse of the housing industry, bond programs can stave off widespread housing price inflation when the economy does recover.

During a time when Congress and the Administration are considering many new and largely untested options for aiding the housing industry, it is ironic that they have not recognized the facts that the MRB delivery system is in place, bond programs are efficient, thousands of first-time homebuyers could benefit and the housing industry could receive a much needed shot in the arm from MRB programs.

Chairman **Gonzalez**. Thank you very much, Mr. Helmbrecht.

I have one question specifically.

Mr. Schechter, I think you made reference on page 5, where you point out, of course, the absolute, and that is that if interest rates are not controlled, everything else becomes what it has been up until now, a bookkeeping exercise. You mentioned that the Credit Control Act of 1969 has provisions that could be taken advantage of in this respect, but I was wondering if you could fill in some specifics. What handle is there in that act that Congress could utilize at this time to control?

Mr. **Schechter**. First, if there were some action toward legislation to extend or make permanent the act——

Chairman **Gonzalez**. I realize it expires in June.

Mr. **Schechter**. Beyond that, the present legislation simply calls upon the President to trigger the action and the Federal Reserve to authorize it. Now, there had been suggestions for additional legislation which would require the President to meet with the Chairman of the Federal Reserve and to discuss it, and so on. I don't know that there can be any legislation to direct the President to do something in connection with the act, because it is a type of legislation where any indication that the legislation might be implemented can cause a run on the bank.

So, if you had to get things moving that way through legislation directing, let's say, some implementation, it would defeat itself. I really think there has to be continued pressure from people outside the Congress and the Congress upon the administration and the Federal Reserve.

Chairman **Gonzalez**. What I was saying was, assuming we could mandate, what would be the mechanics of that mandate? I mean, what specific steps would we be mandating that could be taken under the provisions of this act to control interest rates?

Mr. **Schechter**. There could be certain types of credit which I think are popularly opposed—people are willing to see stopped. For example, corporate takeovers. That has been a fairly big one in the last year. That preclusion, I think if there were a mandate through an amendment to the act or an extension of the act, would begin to have some effect. There could be certain holds on outflows of capital to foreign countries. I believe at one time we even had a tax on foreign bonds being issued in the country.

Chairman **Gonzalez**. That is true. We did.

Mr. **Schechter**. So there are actions which would, I think, meet a certain amount of acceptance and would avoid the use of scarce capital funds for activities which eat up available credit and serve no purpose.

Chairman **Gonzalez**. Thank you very much.

At this time, I may have a question, but I ask unanimous consent to be allowed to submit it in writing.

[The following written question was submitted by Chairman Gonzalez to Mr. Schechter and appears with the response of Mr. Schechter:]

Question. You recommend increasing the authorization for the new rental housing construction program so that more families with incomes below 80 percent of area median may be helped. In designing this bill we have attempted to keep the budget authority for assisted housing within the total appropriated for fiscal year 1982. If we are to keep within those limits and follow your recommendation, how much additional budget authority should we provide for the rental program and which other programs should be reduced to cover those costs?

Answer. I wish to propose two alternative methods of adding more rental units so that families with less than 80 percent of area median can be helped. As spelled out in alternative method I, the AFL-CIO "Alternative to Reaganomics," reproduced below, would increase revenues instead of cutting program budget authority. As you will note, there are specific provisions to undo some of the excessive tax giveaways that were enacted in 1981, as well as to close some long-standing tax loopholes that could raise revenue for a substantial increase in low-income rental housing authorization.

If, however, the committee feels that it must remain within the total budget restraint established earlier, I would strongly recommend the redesign of parts A and B of the new housing production initiative in title III of the bill, as shown below in alternative method II. .

The redesigned program would provide a substantial increase in low-income rental housing, with relatively modest reductions in the numbers of owner-occupied and middle-income rental units. With the same amount of budgetary authority that is provided for the program in H.R. 5731, the redesigned version would be more responsive to the needs of low-income families and produce more rental units which are and will continue to be in tight supply in many market areas.

ALTERNATIVE METHOD I

ALTERNATIVE TO REAGANOMICS

The Alternative provides for: Increase revenues from undoing the worst aspects of last year's tax giveaways, scrutinizing defense outlays and financing any required increases with a corporate and individual surtax, restoration of newly proposed budget cuts, and establishing new jobs programs. It points out ways to raise additional revenues by closing specific tax loopholes:

INCREASED REVENUES

Increased Revenues from Revisions of Tax Law

	Anticipated Revenues (in billions)
Cap the 1982 and 1983 individual tax cuts at $700 per family	$20
Repeal the leasing of tax credits by corporations	8
Repeal the new loopholes in the oil windfall profits tax	2
Modify the widened estate and gift tax provisions	1
Repeal the future indexing of tax rates	—
Total	$31 billion
Increased Revenues from Savings	
Scrutinize defense outlays and finance any required increases with a corporate and individual surtax	
Current proposed defense budget increase	$33
Total	$33 billion
Total of Increased Revenue & Savings	**$64 billion**

NECESSARY OUTLAYS

New Jobs Programs

	Anticipated Expenditures (in billions)
Invest in public infrastructure for the nation's deteriorating communities, including sewer, highway, bridge, mass transit, railroad, and other needed facilities	$ 5
Invest in human capital through effective training of the unemployed and provide public employment opportunities for those who still cannot find work after lengthy searches	5
Encourage low- and moderate-income housing	5
Establish a Reconstruction Finance Corporation to rebuild the nation's industrial base by aiding sectors of the economy and of the country that need special assistance through loans, grants or guarantees	4
Limit harmful imports that aggravate the impact of the recession and weaken key industries	—
Extend unemployment insurance benefits to protect the long-term jobless	4
Total	$23 billion
Restore Budget Cuts	
Restore Proposed Budget Cuts	41
Total	$41 billion
Total New Jobs & Restoring Budget Cuts	**$64 billion**

ADDITIONAL REVENUES

Additional Revenue Raising Proposals
Achieved by Closing
Specific Tax Loopholes

	Anticipated Revenues (in billions)
Change the foreign tax credit to a tax deduction	$10
Repeal the foreign tax deferral privileges	1
Repeal the tax deferrals of the Domestic International Sales Corporation (DISC)	2
Repeal the immediate write-off of oil and gas drilling costs and the special depletion allowances	6
Reduce the Investment Tax Credit to its former levels	7
Apply the lower corporate income tax rates only to corporations with profits of less than $100,000	9
Phase out the special capital gains exclusions	6
Repeal the special capital gains at death exclusions	6
Total	$47 billion
Total Additional Revenues from Closing Loopholes	**$47 billion**

ALTERNATIVE METHOD II

PROGRAM	BUDGET AUTHORITY		ESTIMATED NUMBER OF UNITS		ESTIMATED TOTAL PER-UNIT SUBSIDY	
	in H.R. 5731	proposed modification	in H.R. 5731	proposed modification	amount	over number of years
PART A						
Assisted homeownership	$3.500 billion	$2.947 billion	95,000	80,000	$36,842	10
PART B						
Rental Units:	$1.300 billion	$1.853 billion	75,000	84,000	-	15
low-income	.367 billion	1.153 billion	15,000	39,000	$29,520	15
middle-income	.933 billion	.700 billion	60,000	45,000	$15,550	15
TOTAL	$4.800 billion	$4.800 billion	170,000	164,000		-

Explanatory notes and assumptions:

(1) Median income of $22,395 (rounded to $22,400), as estimated for family of four, nationally, for fiscal year 1982, by the Department of Health and Human Services.

(2) A national average market rent of $6,000 per year assumed for new units; new apartments completed during third quarter of 1981 and rented within 3 months had a median rent of $345 per month, or $4,140 annually as reported by the Bureau of Census.

(3) Assumed that average low-income renter would have income at 60 percent of median, and that those with above 80 percent of median would also be charged 30 percent of income until their income enabled them to pay full market rent with a lower percentage of income.

HBS:ehb 4/1/81

Chairman GONZALEZ. As I said, you anticipated most of the questions.

I want to thank you so much for the recommendations you have made, which are so constructive to H.R. 5731.

At this point, I will recognize the distinguished chairman of the overall committee.

Mr. ST GERMAIN. I will defer, Mr. Chairman.

Chairman GONZALEZ. Well, then we will go on to Mr. Evans.

Mr. EVANS. Thank you, Mr. Chairman, very much.

Thank you, Chairman St Germain. I appreciate it. I appreciate your being here this morning.

Leon, you almost stuck to the script. I think for you you did a very good job. I appreciate very much your concern.

Let me just make a couple of general comments first, Mr. Chairman, and then I would like to ask a couple of specific questions.

Leon, you talked about small business, and I am concerned about small business. I am concerned that a lot of small businesses are being acquired and merged into bigger businesses. I think small business has been the foundation of our country, because the greater number of people who have an incentive to succeed in this system, I think, the better off we are.

I am also concerned about the defense part of the budget, as you are, and the cost overruns and inefficiency. I recommended to the President that he establish a task force which is called the Private Sector Survey, to scrutinize the inefficiency and the waste in the Defense Department, but I think he should go further, and I have suggested that he establish a goal for that Private Sector Survey task force, a goal of eliminating *x* number of billions of dollars of waste in the Defense Department for fiscal year 1983.

I think that will help the perception and the credibility of the economic recovery program, because it must be perceived as fair by all Americans. If some people feel that they are bearing an inordinate share of the responsibility in fighting inflation and high interest rates and unemployment, then they are not going to accept it, and the psychology surrounding that program is absolutely critical.

I think the program is fundamentally sound. I think we could not continue on the road we were going. I think we needed a fundamental change in direction, but the question is how you change. I believe that Dave Stockman has quite often suggested cuts that are too precipitous. We must have something to fill the gap left when these programs are ended. But a $100 billion deficit is obviously too high. A $50 billion deficit is too high. I think you have to compare them, in all fairness, to the gross national product at the time, to the total economy, and I don't think a $100 billion deficit, although I oppose it, is any higher than we have had relative to the GNP in some previous years. That, however, doesn't make it right.

You said we need to get interest rates down. There is no question about it. If the interest rates don't come down, the economic recovery program does not work, and the only way you are going to get interest rates down, in my opinion, is to continue to make every effort to narrow the deficit.

I have some problems with the expenditure of more money, but I recognize that the homebuilding industry is bearing the brunt of this fight against inflation and high unemployment and interest rates. The homebuilding industry has historically led our country out of recessions. I think it can lead the country out of this recession.

I am trying to look at ways in which we can help the homebuilding industry and help people achieve that American dream without substantially aggravating the budget deficit.

Let me ask you a couple of questions, Mr. Helmbrecht, if I may. You said in your statement that H.R. 4717 would provide about 185,000 moderately priced homes. How much of that would be for single family construction?

Mr. HELMBRECHT. Congressman, that would be that if the Bond Tax Act were allowed to operate, you would have 85,000 units. That would all be homeownership housing. That is a single family figure. The rental figure is not included in that.

Mr. EVANS. Now, if we raise those arbitrage limits to 1.25 percent as you suggest, and I agree that they should be raised to make the mortgage revenue bond approach feasible, how long would it take to implement the program?

Mr. HELMBRECHT. Well, as I emphasized, Congressman, in my statement, I believe that this program is up, it is in place, and it could be initiated very quickly. By that I mean many States I know are poised to issue bonds. They have official statements ready to go. There could be a substantial amount of activity within 30 or 60 days.

Mr. EVANS. That is why I think it would help us substantially in coming out of the recession and letting the homebuilding industry lead the way. It seems to me that we are in a situation where we are trying to get to the hospital for some permanent solution to our problems, but we need some plasma for the patient along the way. Otherwise, we won't get to intensive care. And to use that medical analogy, I think the same thing holds true in the housing industry. The mortgage revenue bond program can provide this plasma, provide a tremendous number of job opportunities for people, and as you said, the mortgage revenue bond approach here would generate about $1.8 billion in taxes at the State, local, and Federal levels.

The builders I have talked to, including Mr. Weiner, have indicated that the mortgage revenue bonds can work, but at a rate of about 15 percent. Is there really a market? That concerns me. In addition to the mortgage revenue bonds, I think we need something else. Now, whether it is Mr. St Germain's bill or whether it is something else, that is the real question. I would like the something else not aggravate the budget deficit.

Why don't we take a look, Mr. Chairman, at the money going from the Synfuels Corporation to Mobil and Exxon and Texaco. They are not having any problems with their profits these days. Let's think about allocating some of those funds to the housing industry to help them. What would you gentlemen think of that?

Mr. SCHECHTER. I would strongly endorse repealing the additional windfall oil profits tax reductions in the 1981 tax bill. I would agree with you, Mr. Evans, we ought to ask for repeal of that. I think it could bring several billion in revenue. I mean, those who would be affected are the same firms you mentioned that have benefited from that tax reduction.

Mr. EVANS. Mr. Weiner?

Mr. WEINER. Absolutely. In addition, I believe that—I think there has to be an effort to hit those people that are not paying their taxes. I think that you, Congressman, pointed out one of the areas, and Senator Biden from our little State of Delaware another. One is the fact that the Coast Guard is being cut at a time when we have a $60 billion underground economy that is sapping our strength, and the other that Senator Biden talked about is the fact that 4 years ago there was only $29 billion being lost because people didn't pay their taxes. Now the estimate is that $72 billion are being lost from the biggies who have been getting away with it. What we have done is cut the number of FBI and Justice Department people and IRS people to go after these guys who are cheating on their taxes.

Mr. EVANS. I think the loophole should be closed. People and corporations should pay their fair share.

Thank you, gentlemen.

Thank you, Mr. Chairman.

Chairman GONZALEZ. The gentleman's time has expired.

In today's Wall Street Journal, it says that income tax cheating could cost the United States $97 billion of revenue.

Mr. WEINER. It went up since yesterday.

Chairman GONZALEZ. But when Congress gave away the Treasury last year, we hadn't had that kind of give-away since Andrew Mellon. The Congress did it in the tax bill. That is when we needed the help, because today we can talk all we want to about trimming costs in defense, but we have to make up, just as you suggest.

Mr. Schumer?

Mr. SCHUMER. Thank you, Mr. Chairman. I will keep my remarks brief.

One of the things that all of us have been wrestling with on this issue, on the rental housing issue, is the percentage of housing that we should set aside for low-income families. What we did is, we put together a total package that helped low-income people in different ways, such as public housing, which is something very important to me, and others but we did not want a program—we wanted one component in the package that could work, to increase housing stock.

So, what we came up with was a 20 percent minimum. It could go higher. We have three different opinions here, and maybe you gentlemen can discuss it. You know, you could bat it around a little bit. Mr. Weiner said he didn't know how a program would work with a 20-percent low-income set-aside. He didn't say it couldn't, but he said he was somewhat skeptical. Mr. Helmbrecht, too, said the low income component ought not to be very high. Mr. Schechter, on the other hand, did not say explicitly that the low-income component was too low, but he said he wished there was were more money to increase the low-income component in rental housing.

What do we do?

Mr. SCHECHTER. You know, as I look at the bill, it is low income, and then it is above middle income, a good deal, that we are talking about. Now, I realize there is probably some hope that there will be some trickle-down effect, but in a tight housing market, particularly, trickle-down is not going to work very well, and I don't see how we can really make this type of division. As the arithmetic showed, you would get maybe 15,000 low-income units and 160,000 above middle income. So, I think that it would be——

Mr. SCHUMER. Let me ask you a question. Have you studied the feasibility of doing projects with a higher percentage of low-income tenants? And you said we should get more money. We would love to get more money, but what we did was we put together a bill that lives within last year's budget limitations. Do you think it would be better to have fewer units for lower income people rather than more units for lower middle income people?

Mr. SCHECHTER. I would like to see the distribution tilt more toward the lower end. As somebody else has said, Mr. Berman earlier today, the ones who were 1 percent below, you know, just getting into the market at this time, will probably be getting in shortly. They have less of a problem than those——

Mr. SCHUMER. Maybe they do in other areas. In many large urban areas, single family homes are nonexistent.

Mr. SCHECHTER. I realize that.

Mr. SCHUMER. And that is the thing that plagues me, coming from an area where rental housing is a way of life for all sectors. You know, we had a councilwoman from Denver, and her belief was that rental housing should be for the very low income people, and that you should put lots of subsidies into single-family homes to help all the middle-class people get into that market.

In my area, and in many areas throughout the country, we are not going to get any single-family housing money except through the regular 235 program, which is small, and we need some help with our rental housing stock.

The record should show he is shaking his head.

Mr. SCHECHTER. I spent the first 21 years of my life in New York City, so I am very familiar with what you are talking about.

Mr. WEINER. I don't think it is only a New York City phenomenon, Congressman, and too often we think of either a New York City problem or a rural problem in Hicksville with less than 500 population. The fact is that the majority of the American people live in communities that are between those poles. My comment about making the 20 percent work simply is a function of the interest rate.

The problem is, and one of the worst things we can do in America—I said in my statement I am a conservative, and I meant that. I am concerned that the Congress and that public programs not only be for the low income, but must recognize the needs for the lower middle income and yes, for the middle income people who today cannot afford a decent home, particularly for the young people who are not yet ready to buy and assume that full responsibility.

My concern was how the 20 percent would work in a very practical way, whether or not we would have to increase the rent for the 80 percent to a level where it would be noncompetitive. But I also said that I want to see an effective low income housing program alongside of this, until the thing works out.

We learned in relay races that you can't pass the baton by just flipping it down the track. You have to run alongside of the guy until the other program works, and that was where I was coming from.

Mr. HELMBRECHT. I would only emphasize, Congressman, that the present trend is geared to the very low income and I think that in the section 8 program one of the benefits of the early part of the section 8 program was to allow for substantial income mix of individuals below 100 percent of median or 80 percent of median and down. The trend seems to be 50 percent of median income and that in essence doesn't argue for any social-economic mix.

Mr. SCHUMER. I appreciate all three comments, and they are helpful.

There is just one other comment I would like to make. I wish some of my colleagues on the other side of the aisle were here. It is very frustrating for some of us to sit here and listen to everybody talking about how they want housing, and then vote for an overall budget that cuts the hell out of housing. Those of us who believe we really must help housing, we need you folks to talk to all the members on this committee and elsewhere and tell them they can't have it both ways. They can't say they want housing and then vote for budgets that don't include any housing money.

Thank you.

Mr. WEINER. I think Congressman Evans' contribution to that was—I am saying I think he gave an illustration of the kind of thinking that we need. There is going to have to be some tradeoffs within the constraints of trying to meet the other objectives.

Mr. FRANK. We need voting, not thinking.

Chairman GONZALEZ. Mr. Chairman, Mr. St Germain, it is an honor to recognize you. I just have one question. Is there a community by the name of Succotash in Rhode Island?

Mr. ST GERMAIN. Well, I think there are those who have thought that there was no such area in the country. However, we indeed are proud to say that we have Succotash Road and Succotash Point, and unemployment there has been rising dramatically. You don't have to go back and say you are better off now than you were 4 years ago. They know already.

Mr. WEINER. We are going to build a turnkey there.

Mr. ST GERMAIN. If you build a turnkey there, the island will sink.

Chairman GONZALEZ. Of course, the President singled out the other day in his protest to the press they are bringing out Succotash and this unemployment problem. I just wondered, because I had heard that there was such a place in the State of Rhode Island.

Mr. ST GERMAIN. We have it.

Chairman GONZALEZ. I thought we had it in Texas. We have everything from Dimebox to you name it, but I found out that it was in Rhode Island, so I just wanted to confirm that.

Mr. Chairman.

Mr. ST GERMAIN. I will defer to Mr. Frank.

Mr. FRANK. On the middle-income question, as I said to Mr. Schechter, I don't think the trickle-down theory makes sense in terms of much of the economic area. We were talking about increasing the housing supply. I think there is something to be said for getting housing built, and one of the tradeoffs is that when you are talking about people who are above the median income, so much a smaller number of dollars will get you a lot more units. I think there has to be a mix, and the approach of the Senate is to do none of it.

But we were talking about the housing stock, I don't want to see a trickle-down thing where we build big mansions, but getting some housing done is helpful to everybody, but I think the logic we all agree on is that a voucher program alone, which is the other end of this, which helps only the very poor in a tight housing market, as you point out, is just an exacerbating factor in some ways. So, a properly balanced program obviously for the poor people who need a much deeper level of subsidy, but I think some subsidy is essential, especially since what we are talking about is a high interest rate situation, which is not the fault certainly of those home buyers.

Let me say I am particularly glad to have Mr. Helmbrecht's reference to this question of the existing stock, because I think that has been one of the things that has been lost, and I think the point you make ought to be kept in the forefront, that we are in danger. I mean, it is not simply the case of not building. We are losing because of really unwise policies of trying to pennypinch a substantial number of units.

I wonder, from the standpoint of the State housing authorities—many of them in Massachusetts and elsewhere are faced with this dilemma—I am wondering what the perspective is from the State housing authorities of Federal policies. What is that doing to some of the moderate housing stocks that the authorities now have some responsibility for?

Mr. **Helmbrecht**. Well, Mr. Frank, I would emphasize, and one of the things that I believe many members of the subcommittee support is the continuation of the flexible subsidy program. That has been extremely useful for both State-financed and HUD 236 middle-income jobs in terms of maintaining those developments, and in particular the subsidy program has assisted State agencies in that fashion in terms of assisting the older jobs that are now running into increased maintenance and operational costs.

Mr. **Frank**. What happens if we cut that out?

Mr. **Helmbrecht**. Well, it would be a problem that would crescendo over the next 5 to 6 years, I think because the demand is so high. We have, for example, a number of units in areas of Michigan where people are paying 80 to 100 percent of their incomes to remain in 236 interest subsidized developments, and I know this is occurring nationwide.

Mr. **Frank**. So if we continue present policies proposed by the administration, it is not simply the cessation of new construction but the loss of an existing substantial stock of subsidized units for people.

Mr. **Helmbrecht**. That is possibly a result.

Mr. **Weiner**. Is the Congressman aware of the fact that they set the most astonishing piece of business I have ever seen in my life? They came out with the new budget proposal and they set a cap for all subsidized housing units in the United States at 3.8 million. They said that at the end of fiscal year 1981 there was in existence, occupied, 3.4 million. That includes existing certificate under sections 8 and 235, you know, the whole thing.

They then say they have 700,000 units in the pipeline, and that they only need 400,000, which is where my statement about eliminating 300,000 came from. But mind you, if you will, think about this. That is at the end of fiscal year 1981. The implication is, since there are 400,000 units that are in the pipeline that will reach that cap of 3.8 million, there will be nothing new either in existing or any other kind for fiscal years 1982 to 1985. Now, how are you going to propose even 40,000 vouchers if you want to keep that cap at 3.8 million?

Now we find a new phenomenon developing. There is discussion in the public housing circles about maybe we need a little demolition, and maybe we need to get those units that need flexible subsidy and others out of the way, and maybe we need to get rid of some of our subsidized stock. So we begin to see a whole pattern developing. Somebody arbitrarily took that 3.8 million limit and is now doing what is necessary in a regulatory fashion not only to squeeze out the 300,000 units, but I would suggest that there may be a whole program afoot to squeeze out all of the additional units in order to maintain that cap.

I wanted to call that to your attention if you had not seen it.

Mr. **Frank**. I had not put the numbers together in exactly that fashion.

Mr. **Weiner**. I have to tell you, it is very shaky and scary.

Mr. **Frank**. Mr. Chairman, I am going to wind up. I would like to say that I am awfully glad to see reference to the FAF, because one of the ways in which they could keep us from taking advantage even of what we are supposed to be able to get right now by cutting off the extension. I will just mention that 40 of us in the House have written to the Secretary, a bipartisan group, urging that we extend the deadline until the end of this calendar year, December 1982, and also that we raise the interest rate to 14 percent.

I would just ask, Mr. Chairman, to make a copy of that letter available for the record, because I think that is another. There are a lot of little ways in which they can cut it off, and we wind up worse off than we are.

Chairman **Gonzalez**. Without objection, so ordered.

[The letter referred to follows:]

Congreſs of the United States

Washington, D.C. 20515

March 19, 1982

The Honorable Samuel R. Pierce, Jr.
Secretary of Housing & Urban Development
451 Seventh Street, S.W.
Washington, D.C. 20410

Dear Secretary Pierce:

We are writing to you on a matter of grave concern regarding the future of the Section 8 housing program.

Last summer you took the very wise step of issuing regulations to implement a Financing Adjustment Factor, for which you deserve much praise. These regulations, however, require a June 1, 1982 construction start and limit the FAF to interest rates no higher than 12 percent. Unfortunately, the conditions which led to the implementation of the FAF regulations--unacceptably high interest rates--continue to persist. Therefore, if the FAF regulations are not amended and extended, we fear that a number of very much needed and worthwhile projects already in the pipeline will be lost.

We are asking that the construction start deadline of June 1, 1982 be extended to December 31, 1982. Furthermore, we believe that the current 12 percent limitation is unrealistically low; the very small number of projects which have been able to take advantage of the current FAF regulations clearly bear out this fact. A 14 percent level would much more realistically reflect current interest rate conditions. We, therefore urge you to amend the regulations in this manner.

As the Department noted only last summer in its justification for the current FAF regulations, this procedure is "urgently needed if owners and State and local finance agencies are to continue to process Section 8 projects. There are now pending before the Department a number of highly desirable project proposals in which there has been a substantial investment of private and public funds. Due to current economic conditions, these project proposals cannot be approved without the procedure provided for in this rule."

We submit that the procedure continues to be urgently needed, that the projects continue to be highly desirable, and that current economic conditions continue to warrant the changes in the FAF regulations mentioned in this letter.

Additionally, we are concerned that the question raised recently by the Council of State Housing Agencies concerning HUD's authority under existing regulations to subject the actions of state housing finance agencies to the overall $1.4 billion ceiling the Department has placed on the use of Section 8 monies for FAF be resolved with deliberate speed.

Secretary Pierce
Page Two

Bruce F Vento
Bruce F. Vento, M.C.

Harold Ford
Harold E. Ford, M.C.

C B Rangel
Charles B. Rangel, M.C.

Edwin B. Forsythe, M.C.

Henry S. Reuss
Henry S. Reuss, M.C.

Jim Oberstar
James L. Oberstar, M.C.

Jim Howard
James J. Howard, M.C.

Pete Stark
Fortney H. (Pete) Stark, M.C.

Millicent Fenwick
Millicent Fenwick, M.C.

Sam Gejdenson, M.C.

Barbara B Kennelly
Barbara B. Kennelly, M.C.

Marge Roukema
Marge Roukema, M.C.

Matt Rinaldo
Matthew J. Rinaldo, M.C.

Don Edwards
Don Edwards, M.C.

Frank Annunzio
Frank Annunzio, M.C.

Parren J. Mitchell
Parren J. Mitchell, M.C.

Norman D'Amours
Norman E. D'Amours, M.C.

Joe Minish
Joseph G. Minish, M.C.

Norm Dicks
Norman D. Dicks, M.C.

Vic Fazio
Vic Fazio, M.C.

Wyche Fowler
Wyche Fowler, M.C.

Harold C. Hollenbeck, M.C.

Secretary Pierce
Page Three

Ray Kogovsek
Ray Kogovsek, M.C.

Bill Hughes
William J. Hughes, M.C.

Martin O. Sabo
Martin Olav Sabo, M.C.

Bernard J. Dwyer
Bernard J. Dwyer, M.C.

Mike Barnes
Michael D. Barnes, M.C.

Tony Coelho
Tony Coelho, M.C.

Tom Downey
Thomas J. Downey, M.C.

Steny H. Hoyer, M.C.

Bill Green
Bill Green, M.C.

Larry DeNardis
Lawrence J. DeNardis, M.C.

Toby Moffett
Anthony Toby Moffett, M.C.

Jim Leach
Jim Leach, M.C.

Ed Weber
Ed Weber, M.C.

Les AuCoin
Les AuCoin, M.C.

William J. Coyne
William J. Coyne, M.C.

Chairman GONZALEZ. Mr. Chairman.

Mr. ST GERMAIN. Under the Credit Control Act, Henry, do I understand you correctly that as you know, there is a sunset on June 31. If we were successful in removing that sunset, then the legislation remains in place because it was previously in there. There are those who advocated certain changes in the Credit Control Act. Will your organization be supporting those changes?

Mr. SCHECHTER. We would. For example, we would not want to have again a retroactive—provision for retroactive raising of interest rates on consumers such as has happened in 1980. We are aware of that problem. We might also want to see the mention that there could be some priority identification. What I am thinking of is, we could have a two-tiered limit on credit, 104 percent of credit extended last year, but we will give you another 4 percent for agriculture or housing and exports.

So, we would like to see some room for that, but certainly our main emphasis would be on getting the thing extended, because we think it can be very useful. It proved useful in 1980, and we have foreign experience to back that up.

Mr. ST GERMAIN. Your acuity remains as sharp as it always has been, Mr. Schechter.

Mr. SCHECHTER. Thank you.

Mr. ST GERMAIN. You recognize the realities, and we will try very hard. Also, I want to thank you for your analysis of the Home Mortgage Stability Act, and I will certainly bring your comments—have you submitted these comments to my subcommittee staff?

Mr. SCHECHTER. No, this is the first time.

Mr. ST GERMAIN. Would you be good enough to get together with some of my subcommittee staff on the suggestions that you make? I would be most appreciative.

Mr. SCHECHTER. Sure.

Mr. ST GERMAIN. I don't know if you are aware, but we are going to institute a new version that should be more palatable to the administration. Rather than budgeting money, it will be off budget. We will use network guaranteed certificates, and certainly the administration's projections, if their crystal ball is accurate, then there will never need be any drawing down of funds for the network guarantee certificates.

I wonder if you have given some thought to some new approved certificates. It appears to me that is going to lock them in at 14, 15 percent, and so even though interest rates generally come down three or four points, as far as the money in the thrifts are concerned, we are not going to see that reflected in the home mortgages, because they are going to be locked into those high rates.

Mr. SCHECHTER. And of course what is going to happen is, the additional competitive escalation of different types of intermediaries bidding for the funds, we are going to have all interest rates boosted up higher than they would be. As a matter of fact, it is very much a return to the late twenties, when the depository institutions were bidding for deposits by raising rates, and that was the reason we got the original regulation Q in 1933, right after the decline, because that happened, and we are back in the same position.

Mr. **Weiner**. The Home Loan Bank Board was also part of trying to keep that thing from going out of whack again. We are just sliding right back into some of the worst habits that we saw in the late twenties and in the early thirties.

Mr. **St Germain**. Well, I have just read about what happened.

Mr. **Weiner**. I did, too. I do not remember it.

Mr. **St Germain**. But I cannot disagree with you. It does raise additional concerns because in this subcomittee and in the House, et cetera, we can do our utmost to assist the dilemma of the American public in their quest for housing, but that in itself is not going to answer the bigger problem. The real, real housing is produced not with subsidy but rather in the open marketplace, and that is getting—that picture is getting dimmer and dimmer and dimmer.

Thank you, Mr. Chairman. I realize we have to vote. And thank you, gentlemen. I have a written question to submit to Mr. Helmbrecht, and I may have a few for Mr. Weiner.

[The following written question was submitted by Congressman St Germain to Mr. Helmbrecht, and appears with the response of Mr. Helmbrecht:]

Question. On page 3 of your testimony you mention that non-FAF amendments for section 8 new construction projects must not be arbitrarily capped. Would you explain what the administration is presently doing and why you consider such limitations to be arbitrary? Is the problem the 7¾-percent cap, or the stage in the development process to which this cap applies? What would be a more equitable principle for controlling cost amendments?

Answer. Attached you will find a legal review of our objection to the HUD policy. Let me explain in a summary fashion what we consider to be the problem and the impact of the policy.

Basically the policy limits non-FAF amendments to a 7¾ percent annual increase once a certain stage in the processing of a proposal has been reached. We have been arguing with HUD about that stage in processing and have finally reached an agreement which will lessen the impact of the 7¾ percent per project amendment cap. As originally written, the cap would impact virtually all state and non-state projects and would have reduced the allowable mortgage to the point that the projects would not have been feasible. As currently written, most non-GNMA projects will be able to adjust their cost structure and yet be feasible. Over and above the basic mechanical aspects of the policy is the fact that the cap is nonregulatory and nonstatutory. It is an OMB creation. To enforce the policy, HUD must depend upon their discretionary authority to approve the use of Fair Market Rents of greater than 100 percent.

Another aspect of the cap policy is that there is a national amendment ceiling. State housing finance agencies, until this Administration, have not been eligible for amendment funds, nor have they been subject to a cap. In effect, they were able to use funds appropriated by Congress and assigned to them based upon their own administrative judgment. In exchange, state agencies did not receive new money for amendments. Again OMB decided to upset this balance without a regulatory change. OMB established a new definition for state transfers and considered state agency funds to be under their amendment control. We have legally disputed this fact. HUD seemed to agree, based upon review of general counsel, but by the backdoor they again placed a ceiling on state projects. If a project needs to exceed 100 percent of Fair Market Rents, and most do, then amendments must meet the ceiling restrictions.

It may be that the ceiling will ultimately be a non-issue if either Congress acts to appropriate sufficient funds for amendments, or if HUD and OMB in their administrative and bureaucratic wisdom find a way to fairly apportion ceiling so that pipeline projects can move forward. We doubt the latter will easily come to pass.

Reiterating, HUD and OMB have adopted policies which are contrary to current regulation and are not based upon statutory or regulatory requirements. They intend to enforce these policies via the back-door. It may be possible to work out of this administratively, but it's doubtful. We are working with the House Appropriations Committee and the Senate Appropriations Committee as we trust Congress to resolve the issue as an honest broker.

DUNNELLS, DUVALL, BENNETT & PORTER
ATTORNEYS AT LAW
1220 NINETEENTH STREET, N. W.
WASHINGTON, D. C. 20036
(202) 861-1400

STEPHEN W. PORTER
RICHARD O. DUVALL
G. RICHARD DUNNELLS
TIMOTHY J. BLOOMFIELD
ROBERT S. BENNETT
AUSTIN P. FRUM
CARL S. RAUH
ROBERT E. MADDEN
LLOYD P. GOLDENBERG
GERALD D. LEVINE
ROBERT P. TROUT
BRYAN J. TOMASEK
ALAN KRIEGEL
DENNIS M. HORN
SUSAN R. BARON
ALLAN D. McKELVIE
DAVID M. SCHULTZ
RICHARD NEWMAN

CABLE ADDRESS
DUNALL

WRITER'S DIRECT DIAL

March 3, 1982

John J. Knapp, Esq.
General Counsel
U. S. Department of Housing and Urban Development
451 Seventh Street, SW
Room 10214
Washington, D. C. 20410

Re: State Agency Transfer of Set-Aside v.
Reuse/Recapture Policy

Dear Mr. Knapp:

This is in furtherance of our letter of February 23, 1982 to Mr. Philip Winn (copy attached) concerning the above and responds to your request for additional information concerning the Council of State Housing Agency's (CSHA) request that the Department reconsider its recapture/reuse policies as applied to State Agencies. Specifically, this letter addresses the statutory and regulatory bases which support CSHA's position that State Agencies may freely transfer its previously assigned set-aside funds independently of HUD's present recapture/reuse policies. CSHA's position is further supported, as discussed below, by past practices of HUD, State Agencies and third party developers.

The major legal basis for our position is set forth in our attached February 23rd letter. CSHA would like to reiterate that the State Agency Regulations, 24 C.F.R. Part 883 (the "883 regulations"), on their face, provide sufficient requisite legal justification for excepting State Agencies from HUD's restrictive recapture/reuse policies governing (1) F.A.F. funding; (2) transfers for new units; and (3) contract authority increases.

A. The Statute

In recognition of the "increasingly important and effective role that State Housing Finance Agencies have come to play in the field of government-assisted housing",*/ Congress gave HUD specific authority to set-aside funds for use by State Housing Agencies. Section 213(d)(3), which amends the United States Housing Act of 1937, provides:

> The Secretary may reserve such housing assistance funds as he deems appropriate for use by a State or Agency thereof.

Implicit within this statutory set-aside is the delegation of authority to the State Agencies of certain discretionary powers with respect to their use of set-aside funds.

B. The 883 Regulations

The 883 Regulations govern the processing and procedures which establish the set-aside of contract authority for use by State Agencies. Section 883.101(3) states:

> This part establishes procedures for allocating set-asides of contract authority to State Agencies and sets the policies and procedures under which they must use this authority to provide assistance in newly constructed, substantially rehabilitated, moderately rehabilitated and existing housing.

One of the central findings which must be made in deciding whether to grant set-aside is "the Agency's ability to administer a set-aside so that housing is placed under construction or rehabilitated quickly or assistance is provided in a timely manner. . ." §883.204(c)(1)(ii). This determination, by its very nature, presumes that once a set-aside is granted, State Agencies must be accorded the necessary decision making ability and control over their set-aside to discharge this responsibility. This presumption is confirmed and defined in §883.207 governing Termination and Transfer of Set-Asides. It is noteworthy that the 883 Regulations not only give State Agencies the power and authority to freely transfer its previously assigned set-asides prior to the 45th day before the end of the Federal fiscal year, but also, upon the reporting of certain information to

---

*/ Senate Rep. No. 93-693 on the Housing and Community Development Act of 1974.

HUD, after the 45th day prior to the end of the Federal fiscal year. In each case, "the portion of the set-aside canceled or reduced, will be released and become available for assignment to another project." In pertinent part, the §883.207(c) provides as follows:

> (c) Transfer of Set-Asides. Where a specific portion of an Agency's set-aside is assigned to a particular project (as defined in paragraph (a) of this section) and it is subsequently determined that the portion so assigned cannot be used for that project, the Agency may retain use of that contract authority under the following rules.
>
> (1) Projects terminated or reduced on or before the 45th day prior to the end of the Federal fiscal year. The Agency must notify HUD of any determination to terminate or reduce the contract authority assigned to a specific project. The portion of the set-aside canceled or reduced will be released and become available for assignment to another project through the 45th day prior to the end of the same fiscal year.
>
> (2) Project terminated or reduced after the 45th day prior to the end of the Federal fiscal year. If the determination to terminate or reduce the contract authority assigned to a particular project is made after the 45th day prior to the end of the Federal fiscal year in which the assignment was made to that project, the Agency may transfer the released portion of the set-aside to another project or projects.

Section 883.207(c)(2) goes on to set forth a number of factual reporting requirements concerning the transferred portion of the set-aside (project information) and assurance of AHAP execution within nine months, all of which the Agency must submit to HUD after the Agency determines to make the transfer.

As for the date that set-aside authority is deemed to be assigned, §883.207(a) provides:

> "... set-aside authority is deemed assigned on the date HUD issues a notification of application approval, or a notification of application or proposal acceptance for processing. . ."

From the foregoing, it is evident that once assigned, State Agency funds remain within the Agency's control to be maintained and administered by them. Under all outstanding HUD regulations, transfer authority is reserved to the discretion of the State Agencies with only the specific limitations imposed by §883.207(c) constraining their actions. It is important to note that the only constraints which the regulations impose relate solely to (a) the 45 day fiscal year timing rule, (b) certain factual reporting information, and (c) AHAP execution within 9 months -- the last two of which apply only within the last 45 days of the fiscal year. The clear intent of §883.207(c), confirmed by the absence of any specific limitations in §883.207(c)(1), is to grant the Agencies unrestricted discretionary authority up until the 45th day before the end of the fiscal year.

C. State Agency Reliance Upon Agreements with HUD

The 883 Regulations are tantamount to a contract between HUD and the State Agencies. The contractual relationship imposes certain conditions upon each of the parties, the fulfillment of which gives those parties certain rights and powers. The underlying premise of the 883 Regulation is that in exchange for receiving set-aside contract authority, State Agencies "shall assume responsibility for project development and for supervision of the development, management and maintenance function of owners." §883.201(b). The independence with which State Agencies are expected to discharge their responsibilities under the regulations is reflected by the fact that State Agency certifications are to be accepted by HUD as correct and HUD monitoring is limited to merely insuring compliance with "Federal law and requirements." See §883.201(c).

Once a State Agency has been notified of its set-aside, the 883 Regulations impose the following requirements:

> . . . the Agency must [promptly] make a "public" announcement that it has been allocated a set-aside, specify the amount of the set-aside by housing and household type, indicate where and when applications to the Agency for fund commitments may be submitted by owners. . . The Agency must certify that these notice requirements have been met." §883.204(d).

This notification (NOFA) is published in reliance upon HUD's commitment to make the set-aside funds available to the State Agency for assignment to specific projects. It is at this juncture that the State Agencies are commited to administer the set-aside of contract authority and HUD is likewise commited to make those dollars available to the State Agencies provided they fulfill certain obligations under the 883 Regulations. If HUD's set-aside of contract authority were anything less than a commitment to State Agencies, the Agency's NOFA would be tanamount to misrepresenting the availability of federal subsidies.

By the same token, State Agencies and HUD historically have recognized that the assignment of set-aside monies to State Agencies empowers those Agencies to freely transfer that contract authority to any project or projects within their total set-aside ceiling. In fact, that is the way HUD and State Agencies have always done business and such relationship precedes even the Section 8 Program (witness the Section 236 Non-Insured State Agency Set-Aside Program).

D. Third Party Reliance Upon HF[illegible] Funding "Commitment"

Multifamily housing developers incur substantial costs in reliance upon what they perceive to be a firm State Agency funding "commitment" at the time they receive a Notification of Section 8 Preliminary Proposal Approval. Most developers do not follow the day-to-day submissions and processing procedures between State Agencies and HUD, nor do they rely upon the technical assignment of funds out of the set-aside, which they consider to be a matter between HUD and the Agency. The first firm indication that a developer has a real project "approval" is when he receives notice that the Agency has approved and "funded" his Proposal. Prior to that time the developer has applied to the State Agency for funding and/or financing, processed or received a whole series of state and local approvals, obtained site control and employed numerous professionals to assist in putting together a substantive Section 8 Proposal (architects, engineers, consultants, mortgage bankers, attorneys, etc.).

By the time of Notification of Preliminary Proposal Approval, the developer has typically incurred sizeable expenditures for site options and professional assistance. At this point, the developer usually proceeds to order additional architectural/engineering services, lock up local zoning and other local approvals, determine final financial feasibility, negotiate construction contracts and otherwise prepare the Final Proposal submission to the State Agency, all at a significant additional cost to the developer and his team.

The Comptroller General's opinion of February 16, 1982 (on the question of when Section 8 contract authority is legally commited for purposes of a Federal obligation) as applied to State Agency processing, focuses too narrowly on "final" approvals. Developers typically assume that final approvals will be easily obtained once the preliminary approval is received and once very scarce Section 8 resources have been reserved for them. Moreover, HUD, the State Agency and the developer have them already agreed to the most substantive (and competitive) criteria for Project selection -- rents, overall design, developer capacity and site. Thus the developer has indeed assumed a true Federal and state "commitment" and has expended funds on that basis. The Comptroller General's opinion proceeds all the way from Notification of Application Approval (for Assignment of Portion of Set-Aside to Specific Project) to HUD/Agency Final Proposal approval before recognizing a legally enforceable federal liability. The opinion thus overlooks the earlier (and to the developer, more crucial) stage of Notification of Preliminary Proposal Approval which is the time developers start to incur substantial sums in reliance upon State Agency funding of their Project. To require, as the Comptroller General seems to be suggesting, that all HUD approval authority be exercised before a federal "obligation" occurs, elevates numerous technical and for the most part non-substantitve requirements to a level not usually thought of as fatal to Project processing and fails to recognize the realities of developer reliance upon earlier funding approvals. Moreover, if the Comptroller General's rationale is strictly applied, why would the Final Proposal stage be viewed as the point of commitment, since numerous additional Federal and state approvals are continuously required all the way through initial mortgage loan closing, during the construction period and until final mortgage loan closing.

Finally, it should be noted that the agreement "to keep contract authority available" by HUD and the State Agency, as suggested by the Comptroller General, seems to suggest a much more passive role for the Federal and state governments than that which really occurs. In fact, once the developer receives notice of Section 8 funding, a whole series of meetings and negotiations usually follows during which a number of technical Project processing decisions are made between the developer and the Agency. Developers certainly would not engage in this prolonged process if they did not believe the State Agency to be "commited" to them, with HUD approval.

We hope you will consider the additional information above in making your decision on this matter. We look forward to meeting with you.

Council of State Housing Agencies

By Dunnells, Duvall, Bennett &
and Porter, its counsel.

Gerald D. Levine

Susan R. Baron

cc: Mr. Philip Abrams
Mr. R. Carter Sanders, Jr.

bcc: Tom White
Bob O'Connor
Dick Helmbrecht
John Ritchie

Chairman **Gonzalez**. Thank you very much. Just one question. It will save me having to submit it in writing to Mr. Helmbrecht. That is, in your statement—which I said before, we are very grateful because you had constructive suggestions—you mentioned, though, that in our proposed rental construction section that it be placed on a fair-share equal basis community by community.

But we debated that very much when we were discussing that section, and that is with the fact that it is very limited in amount, did you not think that our judgment that we should target it into the areas of greater need and where the greater use of local resources could be combined, and therefore have a target—target that program?

Mr. **Helmbrecht**. Yes; if there are very limited financial resources I think that is probably the priority you would have to choose. We were centering more on the fair-share program in the previous rental program, which I think was done very equitably and had an excellent balance between rural and urban interests.

Chairman **Gonzalez**. Well, thank you very much and thank you, gentlemen. We deeply appreciate the time you have donated. The subcommittee will stand in recess until 2 p.m. in the main hearing room, 2128.

[Whereupon, at 12:10 p.m. the subcommittee recessed for lunch, to reconvene at 2 p.m. the same day.]

AFTERNOON SESSION

Chairman **Gonzalez**. The subcommittee will please to come to order and we will proceed with the resumption of the hearings begun this morning. And we welcome and appreciate very much the presence and interest of our colleague, Congressman Emerson, and report to him that in view of the fact that I know he has just as pressing a schedule as every one of us, we are going to start off and recognize him, and we are expecting members of the subcommittee to get over any minute now.

So unless you have some reason for not doing so, it would be my intention to recognize you and have you proceed as you see fit.

STATEMENT OF HON. BILL EMERSON, A REPRESENTATIVE FROM THE STATE OF MISSOURI

Mr. **Emerson**. Thank you, Mr. Chairman. Mr. Chairman and distinguished members of the subcommittee, I do most sincerely appreciate this opportunity to appear today before this subcommittee, and I commend you for holding these important hearings on the plight of our housing industry.

Over the past few months, I have had many thoughtful discussions with homebuilders, realtors, mortgage lenders, and prospective homeowners in southeast Missouri. These discussions, along with the frightening statistics that we all know too well, have convinced me that high interest rates have resulted in a housing-sector crisis that demands our immediate attention.

Housing production in Missouri has declined to only 13,000 starts in the entire year of 1981. Unemployment among construction workers is running at over 18 percent, and the failure rate of construction companies across the Nation has increased by 49 percent over the past year. In addition, in my congressional district alone, thousands of young, hard-working families are finding it impossible to buy their first homes.

Indeed, Mr. Chairman, a crisis does exist. However, it is not really productive to merely discuss the statistics that do little but confirm what we already know about the state of the homebuilding industry. I have every confidence that the steps we are taking to reduce the growth of Federal spending and provide long overdue tax relief will help alleviate this dilemma. However, reversing economic trends is a process that takes time, and I am not certain that the housing industry can survive much longer without more immediate action being taken.

I believe that now is the time to act positively and quickly to enact an emergency transition program designed to focus on the immediate problem by temporarily assisting first-time home buyers in the purchase of new but unsold homes.

The program I have proposed is embodied in H.R. 5150, which I introduced on December 9 and which has since gained the support of 55 House cosponsors. Among these cosponsors, Mr. Chairman, are Messrs. Evans, Lowery, McCollum, Coyne, and Dreier, all members of this subcommittee.

H.R. 5150 is designed to provide temporary assistance in bridging the gap between homebuilders who are overburdened with unsold inventories of newly constructed homes and thousands of young, creditworthy families who are willing to buy those homes but are prevented from doing so by prohibitive interest rates.

I call this program the homeownership equity-loan program, or HELP for short. I am confident that this program can provide a meaningful step toward simultaneously relieving the frustrations of potential homeowners and the severe hardships that the housing industry and its employees are facing. Unfortunately, the financing of H.R. 5150 has been a source of repeated frustration for me and the many supporters of this measure.

As you know, Mr. Chairman, I proposed a deferral of the allocation of $500 million from the fiscal year 1982 targeted tandem program. However, in a letter to me dated February 17, Mr. Robert Karpe, president of the Government National Mortgage Association, stated that it was not possible to defer the tandem allocation as proposed in H.R. 5150.

Now, it has come to my attention that during consideration of 1982 administration recission requests, the HUD and Independent Agencies Appropriations Subcommittee has approved the reprograming of $1 billion into the GNMA tandem program. In light of this, I would urge this subcommittee to consider authorizing a half a billion dollars, $500 million, of those funds for implementation of the HELP program.

While it perhaps could be said that this approach is one of Government intervention, it should be made clear that these funds would come out of a recission, and that the legislation provides for recapturing those funds. Moreover, the modest cost of this program would undoubtedly be offset by the increased tax revenue that would result from its stimulating effect on the housing market.

Mr. Chairman and distinguished members of the subcommittee, I know that you share my concern and wish to be responsive to the depression in homebuilding. I respectfully request that to avoid prolonged legislative and regulatory delay, you consider my emergency stimulus proposal contained in H.R. 5150 for separate fast-track legislation action so that aid may be provided by June this year.

I have here a factsheet which I would like to ask permission to have incorporated in the record. Thank you, Mr. Chairman, once again for providing this forum to discuss this problem and perhaps some solutions to our national housing dilemma.

Mr. Chairman, also, I would like to ask permission to insert in the record at this point a letter from the president of the National Association of Home Builders endorsing this proposal.

Chairman GONZALEZ. Without objection, so ordered.

[Congressman Emerson submitted the following material for inclusion in the record: A letter, dated December 7, 1981, from National Association of Home Builders President Herman J. Smith regarding legislation pertaining to the homeownership equity loan program; the text of his bill, H.R. 5150; and a factsheet on H.R. 5150. The material follows:]

National Association of Home Builders
15th and M Streets, N.W., Washington, D.C. 20005
Telex 89-2600 (202) 452-0400

Herman J. Smith
1981 President

December 7, 1981

Dear Congressman:

Legislation will be introduced this week that is intended to stimulate the depressed housing market. Entitled H.E.L.P., the Homeownership Equity Loan Program, the bill would bring down the interest costs for first-time homebuyers who are currently priced out of the housing market.

The volatile and record high interest rates have saddled the market with over 284,000 single-family and 180,000 condominium units that are unsold. This bill would be targeted to sell that inventory.

Today the housing industry, and the thousands of suppliers and contractors are in the 36th month of continual decline. Unemployment in the building industry totals over 918,000 and an additional 200,000 self-employed individuals are without jobs. The failure rate among construction firms is up 41% over 1980 and subcontractor bankruptcies are up 120%. Since the slump began in 1978, the United States has lost over 2.8 million work-years of employment, $49.2 billion in wages and $15.7 billion in tax revenue.

This bill would lower interest rates to an affordable 12%. Mortgage limits would parallel the FHA limits and mortgage would be available for condominiums. Assistance per unit would be limited to $6,000 and upon resale of the unit the amount of the subsidy would be recaptured by the government. Funding would come from the GNMA Special Assistance Program already appropriated. A potential 100,000 homebuyers could be assisted under this program.

I urge you to co-sponsor and support this needed emergency legislation.

Sincerely,

Herman J. Smith

Herman J. Smith
President

"Where Will Our Children Live?"

97TH CONGRESS
1ST SESSION
H. R. 5150

To authorize, on an emergency basis, the Government National Mortgage Association to provide assistance with respect to certain mortgages secured by newly constructed, unsold homes.

IN THE HOUSE OF REPRESENTATIVES

DECEMBER 9, 1981

Mr. EMERSON (for himself, Mr. LOWERY of California, Mr. MCCOLLUM, Mr. GOLDWATER, Mr. NAPIER, Mr. SPENCE, Mr. WHITEHURST, Mr. CLAUSEN, Mr. MOORHEAD, Mr. THOMAS, Mr. DANNEMEYER, Mr. DORNAN of California, Mr. BURGENER, Mr. ROUSSELOT, Mr. PASHAYAN, Mr. NOWAK, Mr. ROBERTS of South Dakota, Mr. ROE, Mr. PRITCHARD, Mr. SHAMANSKY, Mr. DREIER, Mr. HANSEN of Idaho, and Mr. DUNN) introduced the following bill; which was referred to the Committee on Banking, Finance and Urban Affairs

---

A BILL

To authorize, on an emergency basis, the Government National Mortgage Association to provide assistance with respect to certain mortgages secured by newly constructed, unsold homes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 305 of the Federal National Mortgage Associ-

BEST DOCUMENT AVAILABLE

ation Charter Act is amended by adding the following new subsection at the end thereof:

"(l)(1) Notwithstanding any other provision of law, the Secretary of Housing and Urban Development may, during fiscal year 1982 and after taking into account the conditions and purposes described in subsections (a) and (b), direct the Association to implement the provisions of this subsection.

"(2) Whenever the Secretary issues a directive under paragraph (1), the Association shall, in accordance with such directive, provide financial assistance to mortgagors by—

"(A) making commitments to purchase and purchasing the mortgages of such mortgagors and servicing, selling (with or without recourse), or otherwise dealing in such mortgages; or

"(B) making payments to mortgagees, on behalf of such mortgagors, in the form of—

"(i) reductions of the principal obligations of mortgage loans made to such mortgagors; or

"(ii) prepayments of the interest which would otherwise be due with respect to such loans.

"(3) The purpose of such financial assistance shall be to reduce the mortgagor's payments for principal and interest to an amount which would be paid if the interest rate charged with respect to the mortgage were 12 percent per annum.

"(4) Such financial assistance may be made only if—

"(A) the mortgage is a first mortgage secured by a dwelling unit (including a unit in a condominium or cooperative project) designed principally as a one-family residence;

"(B) the construction of the dwelling unit described in subparagraph (A) began (as determined by the Association) before October 1, 1981;

"(C) such unit has not been purchased or occupied prior to the purchase assisted under this subsection;

"(D) such unit is to be occupied by the mortgagor as the mortgagor's principal place of residence;

"(E) the mortgage is insured under section 203 or 234(c) of this Act, or guaranteed under title V of the Housing Act of 1949, chapter 37 of title 38 of the United States Code, or insured by a qualified private insurer as determined by the Association;

"(F) in the case of a mortgage insured by a qualified private insurer, the mortgage meets the terms and conditions applicable to mortgages insured under section 203 or 234(c), as the case may be, of this Act with respect to the maturity term of the mortgage, amortization and down payment requirements, the requirement of an approved mortgagee, and the limitations imposed on the interest rate and the principal amount of the mortgage; and

"(G) the agreement to provide assistance meets other requirements which may be established by the Association as necessary to carry out this subsection in an efficient and effective manner.

"(5) Upon the disposition or refinancing of the property by any mortgagor assisted under this subsection or in any case in which the mortgagor ceases to occupy the property as the mortgagor's principal place of residence, the Association shall provide for the recapture of an amount equal to the lesser of—

"(A) the amount of assistance received by the mortgagor as a result of this subsection; or

"(B) an amount at least equal to 50 percent of the net appreciation of the property, as determined by the Secretary.

For purposes of subparagraph (B), the term 'net appreciation of the property' means any increase in the value of the property over the original purchase price, less the reasonable costs of sale, the reasonable costs of improvements made to the property, and any increase in the mortgage balance as of the time of sale over the original mortgage balance due to the mortgage being insured pursuant to section 245. In providing for such recapture, the Association shall include incentives for the homeowner to maintain the property in a marketable condition. Notwithstanding any other provision of law, any such assistance shall constitute a debt secured by the property to the extent that the Association may provide for such recapture. The amount of any recapture made under this subsection may not be expended without approval in an appropriation Act.

"(6) In issuing any directive pursuant to paragraph (1), the Secretary shall provide that—

"(A) the assistance provided under this subsection is allocated among the various regions of the country on the basis of the inventory in each such region of unsold, newly constructed homes with respect to which assistance may be provided under this subsection;

"(B) the amount of assistance received by any mortgagor as a result of activities authorized by this subsection shall not exceed $6,000; and

"(C) a priority is given to providing assistance with respect to mortgages secured by dwelling units which—

"(i) are modest in design;

"(ii) have been, or are being, constructed by homebuilders whose credit resources are restricted by the small size of their homebuilding operations; and

"(iii) are purchased by families or individuals who have not previously purchased a dwelling unit and who likely would not be able to afford to purchase the dwelling unit without the assistance provided under this subsection.

"(7) The authority of the Association to enter into commitments to provide assistance under this subsection shall expire at the close of fiscal year 1982.

"(8) The Association shall provide assistance under this section by utilizing not more than $500,000,000 of its authority to provide assistance under this section in fiscal year 1982 with respect to projects which are not assisted under section 8 of the United States Housing Act of 1937.

"(9)(A) The provisions of the constitution of any State expressly limiting the rate or amount of interest, discount points, or other charges which may be charged, taken, received, or reserved by lenders and the provisions of any State law expressly limiting the rate or amount of interest, discount points, or other charges which may be charged, taken, received, or reserved shall not apply to any mortgage which is assisted under this subsection.

"(B) The provisions of subparagraph (A) shall apply to mortgages made or executed in any State until the effective date (after the date of enactment of this section) of a provision of law of that State limiting the rate or amount of interest, discount points, or other charges on any such mortgage."

SEC. 2. Section 302(b)(1) of the Federal National Mortgage Association Charter Act is amended by inserting "or a mortgage purchased under section 305(l)," after "or Hawaii," in clause (3) of the proviso in the first sentence.

HOMEOWNERSHIP EQUITY LOAN PROGRAM (H.E.L.P.)

FACT SHEET

1. Program participation is limited to credit worthy first-time homebuyers.

2. Eligible homes are limited to recently constructed or partially constructed and unsold residential properties (single family, condo, or co-ops). A priority is established for lower cost no frills home design (below $67,500).

3. Mortgage financing may be either FHA (203b and 245), VA, private or conventional.

4. Maximum mortgage limit up to 133 1/3% of the FHA Section 203b ($67,500) limit for single family (111% for condo) for each geographic area as determined by the Secretary of HUD. Mortgage term for up to 30 years; down payment required -- same as FHA Section 203b.

5. Interest rate to homebuyer established and based upon income necessary to qualify for the loan as determined by the Secretary of HUD. Rate of interest shall be fixed at 12 percent per annum.

6. The total value and cost of the Federal contribution will be retained and recaptured at time of sale, disposition, or refinancing of the property.

7. The program authority expires one year after date of enactment.

8. A potential of 100,000 unsold homes can be sold and occupied by first-time homebuyers under this program.

9. The Federal cost of providing a temporary and fully refundable loan differential to qualified and working first-time homebuyers for the Federal government would be approximately $500 million for 1982 only. The source of funding will be obtained from previously authorized and appropriated HUD program funds from 1982 through the GNMA Special Assistance program, previously appropriated but not obligated and earmarked for use as interest subsidies for unsubsidized and moderate income targeted tandem projects. The recapture and subsequent loan repayment funds which are repaid to the Federal government through resale or refinancing reuse is made subject to approval in appropriations Acts.

10. Allocation of loan funds by HUD will be made on a regional or State unsold inventory supply basis with a priority established at regional or area basis for the small homebuilder.

11. Homes must be previously unoccupied and for permanent full-time residence of purchasor only.

12. The Government National Mortgage Association (GNMA) is authorized to provide assistance through a mortgage purchase program or by providing direct front-end lump sum payments to financial institutions on behalf of approved and eligible first-time homebuyers for principal or interest write-downs up to a limit necessary to lower mortgage interest rates to 12% for up to a maximum of $6,000, whichever is lower.

Chairman **Gonzalez**. I don't know if you had an opportunity to review one of the two bills that we have before us in the consideration of these hearings; that is, H.R. 5731 and what we suggested there with respect to the tandem program, which as you know, the President's budget zeroes out.

So, what we have here is a fight for survival. Of course, I know you are referring to the recission and with what is on now, but let me assure you that I have followed your legislation and I think part of it, of course, was referred to Ways and Means, part of the kit. I think you have more than one bill.

Mr. **Emerson**. There are certainly many housing bills pending, and I am deeply concerned about this problem. In fact, I am a cosponsor of a number of bills designed to relieve the plight.

Chairman **Gonzalez**. Well, I wanted to tell you that I welcome that, and really, as I said earlier, we deeply appreciate your presence and interest in this very, very critical area. And your recommendation, of course, is going to be very seriously considered here by the subcommittee.

At this moment, though, I was just wondering if you were familiar with this H.R. 5731, which is the vehicle that we have before us. Mr. Lowery?

Mr. **Lowery**. Thank you, Mr. Chairman. Congressman Emerson, you are to be commended for both your efforts and your concern in initiating this proposal. Although modest, I think it is a very effective short-term, cost-effective program to aid first-time home buyers and small business builders, construction workers, homebuilders, and suppliers. As a matter of fact, your bill is actually constructed to address the most critical and disadvantaged segment of the industry; those homebuilders who because of the small size of their operations are suffering rather severe financial hardship as well as potential homebuyers now denied homeownership opportunities because they have no equity ownership.

As you know, other alternatives have been proposed. They offer, I think, more of what can be described as a shotgun approach and do not target the assistance to those most in need, which your bill, H.R. 5150, does. This being the case, wouldn't you agree that H.R. 5150 provides a higher public policy purpose for Federal support, and therefore, should, in fact, as you have indicated, be expedited? And a followup question—do you have any suggestions on how this legislative consideration can be accelerated so that the program will take effect in June while builders are still alive, if you will, although holding on by their fingernails?

Mr. **Emerson**. I am grateful for the comments of the chairman, Mr. Lowery, who assures me that this legislation will receive the consideration of the subcommittee in markup.

I have, in my statement, asked that it be put on a fast track for the very reasons which you suggest, and I hope that that may be done.

Mr. **Lowery**. Thank you, Congressman, thank you, Mr. Chairman.

Chairman **Gonzalez**. Thank you, Mr. Lowery, and thank you, Congressman, again. And of course, we will continue to be in communication with you.

Mr. **Emerson**. Thank you, Mr. Chairman, and I look forward to working with you. If there is any way at all that I can cooperate with the subcommittee, I want to do that. Thank you.

Chairman **Gonzalez**. Thank you very much. We will be in communication with you.

We have next the first panel for this afternoon's hearing, first, Mr. R. Clayton Jones, who is president of NAHRO; Mr. John A. McCauley, deputy commissioner of the Department of Housing and Community Development of the city of Baltimore; Mr. Andrew J. Mooney, the executive director of the Chicago Housing Authority; and Mr. Roy J. Cleveland, the executive director of the Navajo Housing Authority.

Mr. **Lowery**. Mr. Chairman, before we begin I have a short statement that I would like to submit for the record.

Chairman **Gonzalez**. Certainly, you are recognized for that purpose. You want to submit the statement at this point in the record?

Mr. **Lowery**. Yes.

Chairman **Gonzalez**. Without objection, the statement submitted by Mr. Lowery will be placed into the record after the opening remarks this afternoon.

[The statement of Mr. Lowery follows:]

STATEMENT OF HON. BILL LOWERY IN SUPPORT OF H.R. 5150

Thank you, Mr. Chairman. I appreciate you including consideration of this legislation in these hearings.

And thank you, Mr. Emerson, for appearing before this subcommittee today to present our alternative proposal to be of assistance to the housing industry, the unemployed construction worker and the potential first time homebuyer who is currently financially unable to purchase a home.

I am particularly pleased to be a cosponsor of H.R. 5150, the Homeownership Equity Loan Program, because I feel this legislation is directly responsive to the current difficulties of the housing industry. The HELP bill authorizes an interest write-down to 12 percent—the figure generally considered appropriate to stimulate the market. This measure is narrowly targeted to get the biggest "bang for the buck" for our federal tax dollars. Assistance would go to creditworthy first-time homebuyers on an owner-occupied basis to purchase inventory homes. Small homebuilders would get priority. The allocation of these funds by HUD would be made on a regional or state unsold inventory basis. Implementation of H.E.L.P. would mean that 100,000 homes that are currently unsold could be occupied by first-time homebuyers.

Additionally, I am pleased that H.R. 5150 is responsible legislation—the proposal provides for the full recapture of federal funds upon sale or refinancing of the property. This legislation will actually save money for the American taxpayer because defaults, bankruptcies and construction labor unemployment costs can be alleviated, thus generating additional productive capital investment and Federal, State, and local tax revenue.

I strongly urge that this measure be adopted as soon as possible.

Mr. **Lowery**. Thank you, Mr. Chairman.

Chairman **Gonzalez**. Is there any member of the panel who is under a time constraint or pressure, because we will be glad to recognize you first, if there is no objection. If not, if there is no objection, I intend to recognize each one of the panelists in the order that we introduced you, beginning with Mr. Jones and proceeding counterclockwise to the left.

Mr. Jones?

STATEMENT OF R. CLAYTON JONES, PRESIDENT, NATIONAL ASSOCIATION OF HOUSING AND REDEVELOPMENT OFFICIALS

Mr. JONES. Thank you, Mr. Chairman and members of the committee. My name is R. Clayton Jones, I am executive director of the Pontiac, Mich., Housing Commission and president of the National Association of Housing and Redevelopment Officials. I appreciate this opportunity to appear before you today. I have a prepared statement which I would like to submit for the record. I would also like to submit a copy of NAHRO's analysis of the administration's fiscal year 1983 budget request.

Chairman GONZALEZ. Without objection, so ordered.

Mr. JONES. Thank you, Mr. Chairman. Since the administration has yet to submit its legislative package, I request that we be permitted to provide further comments when that package is available.

Mr. Chairman, we would like to thank you and the members of the committee for taking the leadership in putting together a comprehensive housing package. Your package deals effectively with all aspects of the housing crisis, not just isolated issues. At a time when the administration appears to be saying that decent, adequate housing is none of the Government's concern, you have put forth a proposal that clearly reaffirms this Nation's longstanding commitment to decently house its citizens. We thank you and we will do all that we can to support your efforts.

We have commented upon various aspects of your bill in our written testimony. We strongly support your efforts to continue the CDBG and UDAG programs at the currently authorized levels. We applaud your commitment to provide continued funding for public housing development and to initiate a new, creative rental housing production and rehabilitation program.

We have commented on each of these in our written testimony. However, I would like to focus my comments on the most significant crisis still facing us: public housing operating subsidies.

NAHRO represents a body of committed public officials who are responsible for managing over $70 billion in public assets in over 2,700 communities. We house over 3 million people. The people we serve—the elderly, the handicapped, and the large, poor families—are the very persons for whom we have created a "safety net" in this country, and public housing is a part of that "safety net." Today, we represent a body of public officials and agencies straining desperately with minimal resources and under harsh conditions to sustain a viable program.

Over the past several years we have had to make choices which we do not like. They are contrary to our basic principles. We have agreed to sacrifice some housing development funds for operating needs, while we know there is a crying need for housing production in this country. We have agreed to forego public housing modernization funds in order to get funds to handle our day-to-day operations, knowing that deferring needed physical improvements is costly in the long run.

We have made these choices in desperation because the most important thing right now is to pay for the lights and heat, keep the water running, keep the doors and windows working, and to provide a minimal level of health and safety for low-income households that occupy public housing. These immediate needs cannot be postponed. But I must say to you it is sad, indeed, to stand by and watch 90,000 units of desperately needed housing fallen into disrepair and vacancy, and to know that another 100,000 units will soon be in that category and unable to be used by the tens of thousands who cannot find affordable shelter.

That is where we are. We must have the operating funds which our testimony calls for. We have got to have the modernization funds if we are to protect this enormously valuable public asset; we cannot wait for months on end to get the money.

Fiscal year 1982 is almost half over. Local public housing agencies are still not certain what their Federal assistance will be. Many local agencies are one-fourth of the way into their program years and do not know how much money they are going to have. This sorry circumstance again forces us to ask for less than we know is needed.

This we are requesting a certainty of funding in operating needs, even though it may be inadequate. It is not a happy choice, but it is better than the choice we have and the hand-to-mouth uncertainties of the present system.

Most of the members of this committee are familiar with NAHRO's proposal for public housing operations. In essence, we are asking for two things. First, we are asking for a 3-year funding commitment to lend stability to the program, as is done in the section 8 existing and other housing programs. This commitment would enable us to receive funds on a timely basis and be able to plan our activities a year or two ahead.

This predictability is so critical to NAHRO that we are willing to accept a flat 3-year allocation in exchange for a long-term commitment. Although this is clearly less than we need, it is more than we have been getting.

Second, we are asking that housing authorities be given the flexibility to manage their own affairs. Housing authorities should be permitted to develop their own rental and management structures to fit their needs. Local plans should be developed in consultation with tenants and others in the community rather than dictated by a national formula. We must get out from under the disincentives and stifling limitations of the current system.

We are also asking for flexibility to manage our own local circumstances and to find other resources when the Federal share in public housing falls short. We are asking for less than the evidence supports in order to get certainty and the flexibility to deal with our own circumstances.

The public housing crisis continues. Units continue to deteriorate. Tenant services are vanishing, and housing authorities are getting closer and closer to the brink of bankruptcy. We are beginning to feel like a broken record, Mr. Chairman. I do not know what it will take to bring this message home to those who would reduce public housing resources and manipulate funding for other purposes.

Let me conclude by repeating that local, public housing officials take their responsibilities very seriously, striving to serve those who public housing is intended to serve, as well as maintain and improve a very valuable public asset. We have gone about as far as we can go. We must have reform in the operating funding system; we must have flexibility and incentives to be creative and effective. We must have funds to modernize and protect the existing units.

But lest it be too easily forgotten in our desperation to keep our doors open, we must also strive to regain a national commitment to provide newly constructed housing, a well as the tools for economic and neighborhood revitalization. And unless we regain momentum toward these goals, any opportunity to catch up in the years ahead will be irrevocably lost.

We appreciate the strong support our programs have had from this committee in the past, and I know that we will have that support again. Mr. Chairman, thank you. I would be pleased to respond to any questions you have.

[Mr. Jones submitted the following material for inclusion in the record: A prepared statement on behalf of the National Association of Redevelopment Officials; NAHRO's policy analysis of the Reagan fiscal year 1983 HUD budget; NAHRO's comments on the administration's legislative package; and a "Summary of CDBG/UDAG Questionnaire Responses." The material follows:]

STATEMENT OF

R. CLAYTON JONES, PHM,

President

Mr. Chairman and members of the Committee, I am R. Clayton Jones, Executive Director of the Housing Commission of Pontiac, Michigan, and President of the National Association of Housing and Redevelopment Officials. As you know, NAHRO represents over 6,000 individuals and 2,000 agencies involved in carrying out local housing and community development programs. I appreciate this opportunity to appear before you today to discuss housing and community development legislation for fiscal year 1983.

For openers, Mr. Chairman, I would like to congratulate you and your colleagues on the Committee for your housing and community development proposals for the coming year, as contained in HR5731. We applaud the leadership you ve shown in putting together a comprehensive housing package which addresses the myriad of ills facing housing in this country today. We regret that the Administration's legislative package is not yet available, and ask if you might keep the record open so that we can provide written comments after having the opportunity to review the Administration's proposed legislative amendments.

Mr. Chairman, the question we have before us today is a very fundamental one: is this nation going to back away from its 45 year commitment of providing decent, safe and sanitary housing for all Americans? Clearly, the Administration is saying that decent, adequate housing is none of the government's concern; that this belongs within the purview of the private market place. I believe the litany is that "once the interest rates come down, all will be well".

There is no question that high interest rates are severely hampering the housing industry, including the construction of assisted housing. However, acceptable interest rates are not the total solution. Even in the best of economic times, the private sector has not been able to fulfill the housing needs of low and moderate income persons and of deteriorating neighborhoods. Public assistance is essential to provide the basic infrastructure to support housing and to provide housing at affordable rents. I am confident that this Congress understands that basic fact and will reaffirm this nation's long-standing commitment to decently house its citizens.

If we can once clearly reaffirm that goal and responsibility, then we can turn our attention to the best ways of accomplishing our purpose within the tight economic constraints that we face. We believe that you have done exactly that in the legislation that you are proposing. You have retained last year's overall funding level--which reflects a drop of approximately 30% from fiscal year 1981--and yet have provided a balance of programs to ensure viable progress toward our goals.

If I may, I would like to make some specific comments on the provisions of that package as well as on the budget proposals of the Administration.

Public Housing Operating Subsidies

Here we are again, facing a crisis in public housing maintenance and operation. We could undoubtedly simply repeat last year's testimony unchanged because the problems and concerns remain applicable to our current situation: inadequate and unpredictable funding levels, and no local recourse to resolve the problem.

I will not repeat for you the statistics of the public housing crisis, with which you have become so familiar. Rather, we have attached to this testimony a fact sheet on public housing and the results of a recent NAHRO survey concerning the impact of funding cuts on local housing authorities. This data speaks for itself.

We are gratified to see that this Committee's leadership has once again faced the public housing problem squarely and provided $1.6 billion in the HR5731 in order to fully fund housing authorities at the front end. We appreciate the long hard battles that many of you on this Committee fought on behalf of public housing during last year's budget and authorization process, and suspect that we will have a similar, if not even more difficult, fight ahead of us this year.

Thanks, in large part, to yeoman efforts by members of this subcommittee last year, we were able to eke out two supplemental appropriations to bring housing authorities to 96.5% of their funding eligibility for fiscal year 1981. Thus, housing authorities were able to hobble through another year. However, this piecemeal funding of a program which tries to manage and maintain over 1.2 million housing units for over 3 million ~~families~~ people is simply no way to run a ship.

The last of these fiscal year 1981 supplemental funds were distributed earlier this month, after many housing authorities had completed their program years and had already suffered the devastating effect of staff cuts and sharp curtailment of activities.

Now, for the third year in a row, we are starting the year with, at best, 82% of the funds needed to operate our public housing units in fiscal year 1982, and the President is proposing to cut them even further in fiscal year 1983. Housing authorities, that are already one-quarter of the way through their 1982 program years, still do not know how much money they will receive for this year, when they will receive it and under what rules or distribution system.

This is an absolutely untenable situation. It is simply not possible for housing authorities to plan, budget or manage their activities with any level of consistency under these circumstances.

We believe that it is time to rectify this situation. NAHRO believes that it is critical to establish a longer term funding mechanism for public housing operations in order to overcome the devastating effect of the irratic funding situation we now face. We recommend that the funding of public housing operating subsidies be modeled after programs such as the Section 8 existing program, with contract authority provided for the first year and budget authority provided over a period of at least 3 years. Under this system, the Secretary would sign a contract with each housing authority and the funds would be automatically available in each of the three years without the need to seek annual appropriations, except for new units in the inventory.

We understand that our proposal goes somewhat against the tide of the times, when many on Capitol Hill and in the Congress are seeking ways to eliminate long term budget authority and uncontrollable indexing. For that reason, we have kept the term of the commitment short, at only three years. And more significantly NAHRO is willing to accept a flat amount for each of the three years, without indexing for inflation or other cost increases. As you know, Mr. Chairman, this is a rather dramatic position to be taken by this organization that has fought long and hard for adequate inflation factors and full funding of operating subsidies; but it is an indication of how very critical funding stability and predictability is to those who have to manage housing on a day to day basis. Most of them are willing to give up annual funding increases in exchange for being able to plan and budget their activities a year or two ahead and to receive their funding in a timely, predictable manner.

Integrally tied to this proposal is a need to loosen the rules and regulations which hamstring the management ability of housing authorities and provide disincentives for sound management and increasing revenues. Every action of a housing authority is governed by stacks of regulations and reams of forms which drain energy and thwart creativity.

NAHRO's three-year funding proposal would help significantly in removing some of the disincentives. Under this system, housing authorities would receive a set annual amount which would not be reduced dollar for dollar for increases in revenues, as under the current system. Housing authorities, therefore, would have an incentive to creatively seek other resources, both public and private, to help them improve their operations, above and beyond what is provided through the rather niggardly operating subsidy level.

In addition to this flexibility, housing authorities need the ability to establish their own rent schedules in accordance with the needs of their communities, their tenants and their overall operations, subject only to HUD's review. NAHRO is proposing that the flat 30% of income for rent requirement be eliminated, and that housing authorities be permitted to work with their tenants and their local governments in establishing rent and income systems which best suits their circumstances, based upon local housing conditions and the composition of their eligible tenant population.

Under the current system, housing authorities are unable to make even modest adjustments in their rent schedules. If Mrs. Jones lives in a building that is 30 years old, deteriorated, drafty and in a shoddy neighborhood, while Mrs. Smith is able to move into a brand new elevator building with good security and attractive community space, they still pay the same rent if their incomes are the same. The housing authority is unable to provide a differential in their rents, regardless of the discrepancy in the condition of their accommodations. If a tenant's income goes up his rent goes up, even if that rent increase forces him out of public housing; thus, resulting in a disincentive to advance. If a tenant receives a flat welfare payment which includes a shelter allowance exceeding 30% of his income, housing authorities must collect less. If the costs of operating the public housing and providing services to the tenants exceeds the sum of operating subsidies plus income, housing authorities have no recourse but to cut services and watch units deteriorate and/or drop from the inventory.

If we are going to expect housing authorities to properly manage their projects, then we must give them the flexibility to be able to do so.

Most of you on this Committee are familiar with NAHRO's proposal for changing the system of public housing operations. We have attached a summary of this proposal to our written testimony.

We are also aware of the concerns of many of you that there be adequate safeguards to ensure that public housing continue to serve low-income persons within their ability to pay. We share this concern; however, we believe that the system we have now is premised on the worst case scenario, the lowest common denominator; and it is clearly not working. Our public housing stock continues to deteriorate and services to the tenants are vanishing. We believe that housing authorities and their communities can develop better systems to serve the needs of their tenants as well as the physical needs of their properties. Those who cannot should be monitored more closely. Those who can should be given the flexibility to do so.

We are currently gathering examples from around the country of the types of systems that different housing authorities would propose and the impact of those systems upon tenant rents and operating resources, to help exemplify our proposal. We expect to have those collected soon. and would be pleased to share them with the members of this Subcommittee.

I would like to make one final comment with regard to public housing operating subsidies. We noted with interest the provision in HR5731 allowing housing authorities to transfer public housing development funds in the pipeline to cover public housing operations. We had extensive discussions with members of this Subcommittee and your staff last year on a similar provision contained in the Senate version of the appropriation bill; and perhaps now we will say back to you what you said to us at that time: this provision should be approached with caution.

We strongly support the concept, since it provides flexibility at the local level to determine where the greatest need lies and how resources can best be used. It also potentially provides an opportunity for some of the seriously financially distressed authorities to receive an infusion of funds into their operations to help them catch up; something that could never be adequately provided through the operating subsidy system or tenant rents. However, it needs to be made abundantly clear that this is a supplement to and not a replacement for a fully funded operating subsidies system. Otherwise, we will have accomplished nothing more than to jeopardize our public housing production program and to discriminate between those who do and do not have development funds in the pipeline.

Public Housing Modernization

Last year, we outlined for the Subcommittee the potential cost-savings that could be realized through an adequately funded and administered modernization program. Those savings are even greater now as utility costs continue to rise. A fully funded modernization program is a sound investment.

We would strongly urge the Subcommittee not to back away from its original commitment to fund the Comprehensive Improvement Assistance Program at a level of $100 million per year.

There are approximately 200,000 substandard public housing units that could be lost from the inventory if adequate modernization funds are not provided in a timely manner. The longer we delay, or stretch out, the funding of modernization needs, the more costly it will be.

We are pleased to see that HR5731 rejects the Administration's proposal to fund modernization through recaptures and through local options to convert development money. While we support local option, we do not support holding badly needed housing production funds hostage and forcing localities into untenable choices.

The Comprehensive Improvement Assistance Program is a well-conceived and designed program and efforts should be devoted to implementing it quickly and efficiently, not to altering its course.

Public Housing Production

We congratulate the Committee leadership on retaining a viable level of public housing production funds in HR5731. Although the level is only about half the number of units we have had in years prior to 1982, we understand the budgetary constraints within which you are operating and the choices and priorities which must be established.

Although housing construction appears to be in disfavor with many these days, nobody has yet shown us a more efficient, cost-effective way of providing housing for low-income persons, particularly for those with special needs such as large families and Indians. These needs have never been adequately met by the private sector or by other assisted programs and never will be.

While some communities cannot use additional public housing development funds at this time for a myriad of reasons, there are many more communities who are building projects today and could use as many units as they can get tomorrow. Public housing waiting lists of eligible tenants are nearly as long as the list of persons actually served.

We should not back away from our commitment to a program which has been able to provide decent, affordable housing to low-income persons for over 40 years.

Community Development

We strongly support the provisions in HR5731 to fund the Community Development Block Grant and UDAG programs at the levels authorized through last year's legislation of $3.66 billion for CDBG and $500 million for UDAG.

Last year CDBG entitlement communities received funding reductions of approximately 14%; and who knows what will happen to the small cities that have been shifted over to the states? UDAG was cut by 35%. But that is not the worst of it: related programs such as those of EDA and the Small Business Administration and others have been slashed so dramatically that the overall reduction in community and economic development resources available to localities in 1982 was in excess of 50%. If one adds the impact of inflation, the actual reduction is even more devastating.

It is foolish to speak of economic recovery and revitalization and then deny resources to state and local governments to provide the basic infrastructure and incentives to make that recovery possible.

In light of the cuts visited upon community development and economic programs last year, anything less than the authorized levels for CDBG and UDAG would be unacceptable.

NAHRO, the U.S. Conference of Mayors, the National League of Cities, the National Association of Counties and the National Community Development Association, have conducted an extensive survey of cities and counties to determine the accomplishments of the CDBG and UDAG programs and the impact of the actual and proposed funding cuts on program progress and activities. The results of that survey are currently being analyzed and will be submitted to the Subcommittee in the near future. Preliminary data shows dozens of projects abandoned or deferred as a result of the cuts.

We are also pleased to see the continuation of the Section 312 rehabilitation loan program and the Section 108 loan guarantee program in HR5731. The Section 108 program has received accelerated use in recent years and has provided additional up-front capital for community and economic revitalization efforts at virtually no cost or risk to the federal government. It is the type of program that should be continued and expanded in the years ahead as the demand increases.

Section 8 Existing Housing

There has been a flurry of activity over the past year focused on a concept called "housing vouchers". We, as others in the housing industry, worked with the President's Commission on Housing and with HUD in considering how a housing voucher might be designed and what it might accomplish. As this process continued, one feature after another was borrowed from the highly successful Section 8 existing program, until, in the end, what seems to be emerging is a cheap version of that program.

We would ask the question: if the Section 8 existing program is so well designed and successful, why change it? We have heard no one complain that it is a poor program, and few complain about its costs. By reducing the rent standard and eliminating rent increases as HUD proposes, we are only guaranteeing to turn a successful program into an unsuccessful one. At the lower subsidy, there will be fewer adequate units from which to draw, and tenants will be forced to pay higher and higher precentages of their incomes for rent.

To add insult to injury, the Administration is proposing to use the bulk of these units for the conversion of existing leases rather than for adding to the inventory of persons served.

While minor modifications to the Section 8 existing program could be considered, we do not believe that a substantial reduction of the per unit subsidy will result in a workable program.

We support the provisions of HR5731 to continue the Section 8 existing program intact.

Rental Housing Production and Rehabilitation

We commend you, Mr. Chairman and Congressman Schumer, for the introduction of a creative new approach to multifamily rental housing production and rehabilitation.

Although there are those who will produce a flurry of statistics to prove that there is no rental housing crisis in this country, anyone who has tried to rent an affordable unit recently would have some interesting comments on those statistics.

The need for new and substantially rehabilitated rental housing remains acute. Public housing authorities are still able to house only 13% of the qualified population. Waiting lists are extensive. Statistics from HUD's Annual Housing Survey show that, as of 1978, over 7 million households were still housed in substandard or overcrowded conditions; over 3 million households were paying more than 60% of their incomes for rent. As household formations, abandonments and conversions increase, the national rental vacancy rate has fallen well below 5% and in some individual markets it is as low as ½ of 1%. Production of rental housing in the private market has virtually ceased. Short supply and low vacancy rates are putting tremendous inflationary pressures upon the existing housing stock. As moderate and middle-income persons are finding it harder and harder to find affordable units, low income persons are being forced out of the market entirely.

It is imperative that we make steady progress toward providing adequate, affordable housing; and public assistance is essential to that progress.

The NAHRO membership has not yet had the opportunity to review and comment upon your new rental housing initiative, but will be doing so next week at our annual Housing Conference. After we have had the opportunity to discuss your proposal more fully, we would appreciate an opportunity to provide you with more specific comments on its individual provisions.

As an overall comment, however, I will say that I find your proposal to be creative and refreshing. It addresses the very critical need of providing localities and their designated agencies with a tool and an incentive to meet a variety of housing needs, to capitalize on available opportunities, and to do so in the most productive and cost-effective manner.

We would urge you to keep the program simple and to keep overlay requirements and regulations to a minimum in order to preserve these flexible features and allow room for the maximum creativity at the local level.

We look forward to working with you on this proposal in the months ahead.

Closing

Mr. Chairman, I would like to submit for the record along with my written testimony, NAHRO's analysis of HUD's fiscal year 1983 budget request. I would like to thank you for this opportunity to appear before you today, and would be pleased to respond to any questions.

NAHRO
Serving the Nation's Housing and Community Development Needs

THE CRISIS IN PUBLIC HOUSING

NAHRO Fact Sheet
November 10, 1981

Funding Shortfall

- In 1982, approximately 44% of all operating costs will be spent on utilities. Since utilities are fixed costs, funding cuts will all have to come from the remaining 56% of the budget, which covers items such as maintenance, security and administration.
- An independent study completed for HUD by Abt Associates indicated that the performance funding system that is used to determine operating cost levels is inadequate, particularly for large urban housing authorities; and has persistently underfunded operating subsidy needs.
- The fiscal year 1982 HUD-Independent Agencies conference report contains a $148 million supplemental appropriation to help cover the shortfall in fiscal year 1981 funding. The President has requested that this supplemental be deleted; this would result in a maximum operating subsidy funding level of 85.3% for 1981.
- The fiscal year 1982 HUD-Independent Agencies conference report contains $1.205 billion for 1982 operating subsidies, an amount adequate to fund a maximum of 79% of the current need as estimated under the performance funding system.
- The President, on October 1, 1981, proposed reducing the appropriation level by 12% to $1.06 billion, an amount adequate to fund a maximum of 69% of the estimated operating subsidy need.
- Forty-one percent of the operating subsidy funds are disbursed to PHAs with program years beginning on January 1. These PHAs will be forced to operate at the levels appropriated as of December 31, 1981.

The Growing Gap Between Income and Operating Costs

- Operating costs almost tripled between 1968 and 1978, while monthly rent increased less than 50%.

- The cost of the backlog of deferred routine maintenance expenditures was estimated at $400 million four years ago and has increased substantially since then.

- Some $200 million is needed to compensate for HUD's underestimates of inflation and underfunding of operating needs of public housing authorities over the past five years.

- In 1980, public housing agencies spent approximately $750 million for energy costs alone, and energy costs have increased more than 400 percent during the past 10 years.

- Public housing authorities received only 85.5 percent of the operating funds that HUD admits are needed to get them through fiscal year 1981.

Modernization of Existing Housing and Energy Conservation Measures

- 90,000 units require major rehabilitation or it will soon no longer be economically feasible to rehabilitate them. Rehabilitation costs today would be $2.25 billion; replacement cost four years from now is conservatively estimated to be $6.12 billion.

- 110,000 units today require some rehabilitation; and another one million units require basic maintenance.

- $4 billion is required to return all the public housing stock to decent, safe, sanitary and energy efficient conditions and bring all these units into good repair.

- An expenditure of $1,350 per unit for energy conservation would result in an annual saving of $325 per unit. The initial investment would be recouped within four years.

Profile of Public Housing

- More than 3.4 million people today live in 1.2 million units of public housing.

- They comprise some of the most vulnerable in our society -- the poor, the elderly and female-headed households. Median income is $3,718; the elderly occupy 46% of the units; female-headed households account for another 46%.

- At least 5% of the tenants have a serious physical handicap.

- Income of these tenants has increased an average of only 5% per year while inflation has increased in the neighborhood of 10% or more.

- Demand for public housing units is strong. Most projects are fully occupied with waiting lists. Nationally, only 2% of public housing units are vacant.

- Demand for public housing is expected to grow as the poor are now being squeezed out of private rental housing. The private sector rental housing vacancy rate in 1980 was only 5.1% and there was a 30% decline in construction of rental housing between 1979 and 1980.

- Elimination of social service support programs such as the Comprehensive Employment and Training Act (CETA), day care and food stamps, will reduce available income to those at the economic margin and spur demand for public housing.

- The nation has already invested $20 billion on the development of public housing projects since 1937.

- Today's replacement cost for the buildings alone would be $75 billion.

- Some 9,904 public housing projects across the country are managed by 2,700 public housing authorities.

- The average size project is 119 units, about 19 years old, and typically a low-rise structure.

- Of those 2,700 housing authorities nationwide, 152 are considered large, with over 1,250 units under management, accounting for about 60% of all public housing under management.

- By 1975, every large public housing authority was operating at a deficit. Many are on the verge of bankruptcy.

- Thirty-two public housing authorities have exhausted their reserve funds or have depleted more than 80% of their reserves. (This includes Atlanta, Boston, Chicago, Cleveland, Detroit, Houston, Kansas City, Missouri, Newark, New Orleans, Philadelphia, Los Angeles, San Francisco and Washington, D.C.).

Results of NAHRO Survey of 23 PHAs On Impact of Operating Fund Cuts

- All of the PHAs survey will have net operating deficits in fiscal 1982.

- Seventy percent of PHAs surveyed will not have sufficient reserves to cover their projected fiscal 1982 deficit.

- Thirty-five percent of PHAs surveyed indicated they will be forced to close some occupied units and more than 45 percent indicated they would be forced to close units that become vacant.

- Seventy-four percent of PHAs responding have already made significant reductions in maintenance personnel as a result of funding at only 85.5% of need in fiscal 1981.

NAHRO

Serving the Nation's Housing and Community Development Needs

MAJOR FINDINGS, NAHRO SURVEY

November, 1981

NAHRO has conducted a survey of public housing authorities to assess the effects of a PFS funding level of 69% for FY82. NAHRO is adamantly opposed to any additional budget cuts to operating subsidies. It is imperative that PHAs be fully funded for both FY81 and FY82. This means that Congress must direct the Department of Housing and Urban Development to obligate a $148 million supplemental appropriation for FY81 to authorities before the end of this year, and that at least $1.5 billion must be appropriated and allocated in full for FY82 operating costs.

In order to provide Congress, the Administration, the press, and localities with facts, we have been doing extensive research. Thus far, we have information from 26 PHAs representing 30% of the total federally-subsidized public housing stock, with over 365,000 units under management. These authorities vary in size and financial condition--however, all have clearly indicated that a funding level of 69% of need in FY82 will mean disaster for low income people and localities across the country, specifically...

1. Over 311,280 eligible households are currently waiting for federally-funded public housing--just in those PHAs surveyed.

2. Thirty-five percent predict they will have to close units. Although closure is viewed as a last resort by most PHAs, some feel they may have to close entire buildings.

3. Over 84% will have to cut staff. Ninety-five percent expect to cut maintenance, 90% will cut administration, 85% will cut management, 80% of those having security forces will have to cut them, and 70% will have to reduce tenant services.

4. These personnel reductions are on top of staff cuts already taken by 63% of the PHAs as a result of 1981 short-funding.

5. A subsidy shortfall of $162.7 million is expected by the 26 PHAs surveyed.

6. Over 15% currently have no reserves.

7. Seventy-three percent of those PHAs having reserves do not have sufficient reserves to cover their anticipated deficits.

8. Accelerated deterioration, increased vandalism, rent delinquencies, increased vacancies, and problems re-renting units are all very real problems that are expected by every PHA surveyed.

NAHRO
Serving the Nation's Housing and
Community Development Needs

A NAHRO PROPOSAL: RETAINING PUBLIC HOUSING AS A VIABLE AND STABLE HOUSING RESOURCE FOR LOW-INCOME FAMILIES

In October, 1981, the Board of Governors of the National Association of Housing and Redevelopment Officials (NAHRO) made a bold proposal designed to retain public housing as a viable low-income housing program and provide stability in its operations.

Why is the NAHRO proposal necessary? The NAHRO proposal is required because the current mechanisms in public housing operations, put into place over the past 12 years, have created an unworkable and chaotic system: (1) the annual level of Federal operating assistance is uncertain and its time of delivery is unpredictable; (2) the allocation of Federal operating assistance among local public housing agencies produces inequities--with some PHAs receiving funding not required, while others are seriously underfunded; (3) local public housing agencies are currently constrained by Federal statute and regulations from making adjustments in local operations to assure stability in their operations.

What are the basic elements of the NAHRO proposal? The basic elements are three--and they are interdependent.

A 3-year fixed commitment of Federal operating assistance
A return to local PHAs of management control of their own operations
An adjusted, more equitable system of allocation for Federal operating assistance

As the scale indicates, the basic elements of the proposed new system depend on each other--if one is out of balance, the system will not work. All three are required. The fulcrum of the system is the PHA, and its ability to use Federal operating assistance and other resources in the most effective way to meet local needs.

How would the 3-year fixed commitment of Federal assistance work? The Congress would authorize the Department of HUD to contract with local public housing agencies to receive a fixed commitment of funds over a three year period (fiscal years 1983, 1984 and 1985). The funds would be allocated annually at the beginning of a fiscal year. The base for the Federal commitment would be a calculation of the requirement of the Performance Funding System (PFS) for FY1982. Though this amount can be adjusted, the full annual requirement for FY1982 is currently estimated at $1.523 billion.

What is the new mechanism for allocation of Federal operating assistance? The Department of HUD, at the request of the Congress, is preparing an analysis of alternative allocation mechanisms for federal operating assistance due to be delivered by March 1, 1982. This analysis will include calculations of the impact of the various allocation methods on local operations. Following the release of this HUD analysis, NAHRO will make its own recommendations on an allocation system. Once allocated, the Federal assistance would be fixed for a local PHA. No allocation system should involve a reduction of Federal operating assistance if a PHA increased its local income, or reduced expenses due to management improvements. It is recognized that a small number of severely-distressed PHAs would require supplemental assistance in converting to any new system.

What changes are required to remove current constraints on local PHAs in managing their own operations? The Federal statute and Federal regulations need to be amended to authorize PHAs to set local income and rent schedules based on local conditions and needs, subject only to two national requirements: (1) that public housing serve lower income families within the eligibility range (i.e., up to 30 percent of median income in the local area) including families at the lower end of the eligibility range; and (2) that rents be set, taking into account local housing market conditions, and the rent-paying abilities of families of various sizes and income levels within the eligibility range. Schedules would be reviewed by HUD for conformance with these two requirements.

How would the interests of public housing residents be protected? Income and rent schedules would be developed by the PHA after consultation with public housing residents and others in the local community. They would also be reviewed by the Department of HUD. The basic criteria would be: (1) that public housing serve the lower income families within the eligibility range (i.e., up to 80 percent of median income in the local area) including families at the lower end of the eligibility range; and (2) that rents be set taking into account local housing market conditions and the rent-paying ability of families of various sizes and income levels within the eligibility range. The objective would be to keep rents as low as possible while utilizing the available resources and maintaining a sound operation.

How would the NAHRO proposal stabilize public housing operations?

--It would remove the chaotic funding pattern of federal operating assistance which has characterized the last several years; and at the same time, stop the rapid escalation of these operating costs in the Federal budget for the next three years.

--It would insure a more predictable, timely and equitable distribution of Federal operating assistance to local PHAs.

--It would enable local PHAs to manage their operation in a business-like manner, based on local needs and conditions; and with real incentives to make operating improvements.

Serving the Nation's Housing and
Community Development Needs

NAHRO POLICY ANALYSIS

The Reagan Budget for the Department of HUD, FY1983--it not only curtails activity for the short-run; it is a blueprint for the future of HUD.

March 15, 1982

National Association of Housing and Redevelopment Officials
2600 Virginia Avenue, Northwest, Suite 404, Washington, D.C. 20037 (202) 333-2020

NAHRO Policy Analysis March 15, 1982

THE REAGAN BUDGET FOR THE DEPARTMENT OF HUD, FY1983--IT NOT ONLY CURTAILS ACTIVITY FOR THE SHORT RUN; IT IS A BLUEPRINT FOR THE FUTURE OF HUD

The first full budget of the Reagan Administration, that for fiscal year 1983 beginning in October, 1982, was delivered to the Congress on February 8. It reflects not only an intent to curtail spending in most domestic programs for the short run; it is the beginning of a Reagan blueprint for the future of these programs.

In the case of the Department of Housing and Urban Development (HUD), the news is not good. The proposed 1983 HUD budget virtually dismantles all of the Department's programs for new construction of assisted housing for lower income families. It puts "on hold", at a flat level, the budget for HUD's Community Development Block Grant (CDBG) and Urban Development Action Grant (UDAG) programs, pending a potential turnback to the states of these programs in fiscal years 1984 under the Administration's program of "New Federalism". It cuts back the level and scope of activity for the mortgage insurance programs of the Federal Housing Administration (FHA). For on-going operating programs, such as public housing, Section 8 and other assisted housing under management, the budget seriously curtails federal operating assistance. Some existing units would be sold or demolished with no replacement. Eleven HUD programs are not just curtailed; they are eliminated. The level of authorization for policy development and research activity is cut in half from fiscal year 1981.

In the place of these cut-backs and eliminations, there are two HUD budget initiatives. A "modified Section 8 housing certificate" program is designed to replace the current Section 8 existing leasing program, at a reduced commitment of assistance and scope of coverage for lower income households (see Chart I). The second initiative--rental rehabilitation grants--replaces Section 312 rehabilitation loans and Section 8 moderate rehabilitation (see Chart II): under its provisions, the term of assistance would be reduced to five years; local communities would be required to provide half of the cost of rehabilitation; specific federal requirements would govern where grants could be used--even so, the proposed activity is very limited, at a level of 30,000 units.

Given the direction of the cut-backs, eliminations and alternatives in the proposed HUD budget for 1983, the future mission of the Department as a major actor in housing and community development is cast into doubt. The Reagan blueprint appears to be for a greatly diminished federal role in housing and community development.

The success of this blueprint will depend on actions by the Congress on the FY1983 budget proposal--involving the whole range of federal budget issues.

THE 1983 HUD BUDGET: AN OVERVIEW (TABLES 1 AND 2)

The actual HUD outlays for fiscal year 1983 are estimated at only 10 percent less than in the current fiscal year--$13.1 billion in contrast to $14.6 billion. But outlays are only the end result of earlier allocations of budget commitments--the real story is in the request for budget authority. The depth of the curtailment in HUD's activity is starkly clear in the budget authority numbers: a reduction from $33.4 billion in 1981 to $13.1 billion in 1982 to $684.7 million in fiscal year 1983--a total 3-year reduction of 98 percent. Table 1 spells out the detail of these changes over the 3 years.

The deep cut-backs in budget authority are in the authorizations for new construction of Section 8 and public housing from $25.0 billion in 1981 to a net of minus $5.2 billion in 1983 after rescissions. The only new construction reservations scheduled for 1983 in HUD's housing assistance programs are the token 10,000 new units to be reserved under the Section 202 loan program for elderly or disabled persons; even this is a reduction in budget authority of 65 percent over 1981. Yet, even the severe reductions in new budget authority mask the full impact. The 1983 HUD budget achieves reduced numbers by "recapturing" assisted housing commitments already made in prior years; and rescinding a substantial portion of these prior year obligations. In a similar move to cut back new assisted construction activity, the secondary market support supplied by the Government National Mortgage Association (GNMA) through its Section 8 tandem and targeted tandem programs is eliminated in 1983--dropping from annual levels of over a billion dollars each in 1981 and 1982. A key element in the decision to cut back budget authority for new assisted housing construction was undoubtedly the long-term (20 to 30 years) federal commitment involved: concern with the growing base and the multi-year nature of the commitment for housing assistance has been growing in recent years. But the 1983 HUD budget would not only curtail, but essentially eliminate this housing assistance mechanism with no alternative proposed for new assisted construction activity.

While the Community Development Block Grant (CDBG) and Urban Development Action Grant (UDAG) programs are maintained in 1983 at the current year's dollar level ($3.456 billion and $440.0 million respectively), this actually reflects a reduction in activity due first to the inflation in costs; second, in the case of CDBG, to the expanded program eligibility of additional communities and the new split in final allocations using a 70-30 split for entitlement and non-entitlement (small city) categories. CDBG entitlement cities are estimated to grow from 669 to 732 between 1981 and 1982. The impact of all of these changes is a likely reduction in CDBG grants to entitlement communities from 10 to 17 percent. Also hanging over both CDBG and UDAG is the transfer to the States of the administration of small city CDBG programs and the announced intention of the Reagan Administration to transfer these two programs in total to the States in fiscal year 1984 as part of the program of "New Federalism".

There are other prescient signs in the 1983 HUD budget. The Federal Housing Administration (FHA) is subject to a severe curtailment of the authority to make new home insurance commitments--down to $35 billion for 1983. The new budget also assumes the enactment of a wide range of legislative proposals designed to re-direct FHA to serve a more limited clientele, such as first time and inner city home buyers, thus reducing competition with the private mortgage insurance industry. As in the case of the elimination of GNMA's secondary market tandem support for assisted housing, the changes in the FHA program are part of a government-wide effort to reduce the federal government's involvement in credit activities.

As shown in Table 2, eleven HUD program activities would be subject not just to curtailment but to elimination, beginning in 1983: Section 8 new construction or substantial rehabilitation; public housing new construction, substantial rehabilitation or acquisition; regular Section 8 tandem and targeted tandem assistance under GNMA; housing counseling grants (although HUD will continue to certify or recertify counseling agencies); Section 701 comprehensive planning grants; Section 312 rehabilitation loans; Neighborhood Self-Help Development Grants; Section 108 CDBG Loan Guarantees; the Solar Energy and Conservation Bank.

Other HUD programs which survive the most severe curtailments in the 1983 budget are still subject to uncertain futures. The existing inventory of 1.2 million public housing units remains in a chronic battle to survive by obtaining adequate federal operating assistance: the proposed level for 1983 is 17 percent below the 1982 level; it is estimated to meet only 71 percent of the projected need of at least $1.5 billion, the proposed changes in income and rent determination will not accommodate such a shortfall. Also, the 1983 budget calls for the elimination of some 5,000 public housing units considered to be badly-deteriorated and not cost effective; there is no replacement for these lost units. Hard choices will also face local housing authorities who have commitments for new housing construction but find their only funds for modernization of existing units is to trade-off this new construction commitment. The inventory of HUD--Section 8, rent supplement, and Section 236 rent-assisted units is also subject to major changes involving (1) a transfer of most rent-supplement and Section 236 rental assistance payment projects to the Section 8 existing housing program; (2) an anticipation of some "5-year opt-outs" by owners of Section 8 new construction and substantial rehabilitation projects; (3) a reduced volume of assistance in 1983 and no new request for budget authority for the flexible subsidy for FHA troubled projects.

The Section 8 existing housing program, currently providing assistance for over 800,000 households in private rental housing, is scheduled for a phased turn-over to the new "modified Section 8 housing certificate program" as current leases expire over the next five years. In 1983, a total of 60,615 existing housing units would be transferred to the new program. This new certificate program would be subject to a reduced assistance commitment for families, and a reduced role for local public housing agencies.

The end line for all of the changes in HUD housing assistance programs, beginning in 1982, and accelerated in 1983, is to bring the federal commitment for assisted units to a base of no more than 3.8 million units by 1985. The current HUD-assisted inventory is 3.4 million units: public housing (1.2 million units); Section 8 existing housing (844,000 units); Section 8 new construction/substantial rehabilitation (475,000 units); Section 236 moderate rental not receiving operating assistance (342,000 units); rent supplement and Section 236 moderate rental receiving rental assistance payments (207,000 units); Section 235 low-income homeowners (235,000 units); and Section 202 housing for elderly or handicapped (97,000 units).

THE 1983 HUD BUDGET: THE STRATEGY BEHIND THE HANDLING OF BUDGET AUTHORITY

The strategy behind the 1983 HUD budget handling of budget authority for assisted housing is clear: to reduce long-term federal obligations for housing assistance payments on existing contracts; and to eliminate any new obligations for future payments for any new units in the production pipeline which are not firmly under contract. The strategy, in short, is to curb to the maximum degree possible the growth of federal support for assisted housing.

The multiple actions involved in reducing federal "pay-out" obligations in future years are basically five: (1) reducing the term of federal payment obligations, where possible, of projects already under contract; (2) conversion of existing leasing obligations; (3) eliminating some assisted housing units from the inventory by disposition or demolition; (4) increasing tenant rent contributions; and (5) honoring only those units in the production pipeline which have firm (contractual) obligations. In budgetary terms, the first three actions have the result of "recapturing" previously committed budget authority, part of which is permanently rescinded.

Tables 3 and 4 spell out the full budgetary program for the availability and utilization of budget authority for Section 8 and public housing in fiscal years 1982 and 1983. In 1982, the proposed budget estimates the recapture of $7.5 billion in previously committed budget authority; and in 1983, the recapture of $9.9 billion in budget authority. Of the total budgetary authority available in 1982, $9.4 billion or 34 percent is proposed for rescission; in 1983, the figures are $2.4 billion or 24 percent. These figures are exclusive of rescissions for the rent supplement program of $2.8 billion in both 1982 and 1983.

Table 3 also documents that of the net authority available after rescissions in 1982 ($18.3 billion), the largest proportion (43%) goes for the conversion or disposition of existing housing projects; smaller proportions (20% and 16%, respectively) go for amendments to new activity in process; and for new commitments for future development. Budget authority is also set aside for modernization of existing public housing, and to cover interest differential payments involved in the sale of public housing obligations to the Federal Financing Bank.

In 1983, Table 4 shows that of the net authority available after rescission ($7.5 billion), the largest proportions (24% and 23%, respectively) go for modernization of public housing and amendments to new production activity in process. Approximately equal proportions (19% and 17%) go for the sale of public housing obligations to the

Federal Financing Bank, and to new reservations for 10,000 units of Section 202 housing for elderly or handicapped persons. Also, the new program of modified Section 8 certificates is assigned 14 percent of available budget authority to support 30,000 new units in conjunction with the new rental rehabilitation grant program.

REDUCING FEDERAL OBLIGATIONS

The strategies behind these actions require some further explanation.

Reducing the Term of Federal Obligation

The prime examples of this strategy are in the handling of existing rent supplement projects and Section 236 projects receiving rental assistance payments, representing a current inventory of 160,000 and 13,000 units respectively. It is proposed to reduce the federal commitment from the 20 to 40 year contracts now in existence to the maximum 15-year term under the Section 8 existing housing program. The "recapture" of budget authority is the difference between the new 15-year term and the previous 20 to 40 year obligations. It is also anticipated that some 34,700 units of state-assisted non-FHA insured housing will not be converted, and any additional assistance will become the obligation of the States. While the full budgetary authority is reserved in 1982, it is anticipated that the conversion process will require a 3-year period for the rent supplement units--60,000 units each in 1982 and 1983, and 40,000 units in 1984.

Another example of this strategy is in the conversion of Section 8 existing housing units (with 15-year budget authority) to the modified Section 8 housing certificate program (with 5-year budget authority). A total of 60,615 Section 8 existing units are programmed for such conversion in 1983.

Disposition of Existing Project Obligations

An example of this strategy is the use of Section 8 authority for the disposition of an estimated 10,000 units in HUD-owned multifamily projects. Another example is the elimination of the long-term federal commitment for Section 8 new construction projects where the owner exercises his right not to renew the contract at the end of a five year contract period; 1000 units each are estimated in this category in both 1982 and 1983. A still further example is the proposed sale or demolition of an estimated 5,000 public housing units in 1983, where it is determined not to be cost-effective to rebuild deteriorated units. In all of these examples, long-term budget authority would be recaptured.

Conversion of Existing Leasing Obligations

These conversions fall into two categories. The first is the continuing process of converting the original Section 23 leases to the Section 8 existing housing program, estimated at 5,000 units in both 1982 and 1983. The second is the beginning of the conversion of leases under the Section 8 existing housing program to the new modified Section 8 certificate program, estimated at 60,615 units in 1983; this latter program has a significantly lower federal cost.

Use of Leases to Assist Families Displaced from Existing Assisted Projects

Section 8 leases are used for this purpose in both 1982 and 1983, in the instances of families residing in Section 8 new construction where the owner does not renew the five year assistance contract, and of families residing in public housing units which are sold or demolished. Families residing in HUD-owned projects where disposition takes place will receive modified Section 8 leases. These lease commitments are less costly to the federal government than long-term contracts related to new construction.

Phasing Out Current Operating Assistance

This process refers to FHA-troubled projects which have been receiving the "flexible subsidy" for short-term assistance with operating deficits. The 1982 budget anticipates a final use of budget authority and a transfer from the rental housing assistance fund, spread out over two years, with 148 eligible projects receiving assistance in 1982 and 98 eligible projects in 1983. This assistance will be restricted to projects with FHA insurance; it will not cover non-insured projects developed by state housing finance agencies--it is anticipated that any operating assistance on these projects will come from the States.

Increasing Tenant Rent Contributions

The HUD budget anticipates changes that will further raise rent contributions of families in assisted housing, thus reducing federal operating assistance. These changes include:

(1) implementing the increase in rent-to-income ceiling from 25 to 30 percent, at a rate of one percent of income per year beginning in 1982.

(2) requiring all new residents to pay 30 percent of income.

(3) counting the cash value of food stamps as income in assisted housing (this would require a legislative change).

(4) discontinuing the payments to residents of assisted housing where monthly utility bills exceed 25 percent of their adjusted incomes.

(5) increasing the limit on the rate of annual rent increases from 10 to 20 percent (this will require a legislative change).

MODERNIZATION OF PUBLIC HOUSING

In both 1982 and 1983, budget authority is authorized at the level of current commitments--$1.8 billion in each year. This is estimated to be sufficient to finance $981.9 million of capital improvements in each year. This action is in harmony with the Administration's goal to support existing housing. However, the budget authority for this program is not new--it is recaptured from previous authorizations. In 1982, $300 million of budget authority is deferred from 1981; $1 billion is from normal recaptures of public housing development funds; and $500 million is from recapture from public housing agencies accepting the HUD offer to use 50 percent of its reserved development authority for modernization. In 1983, the budget authority for modernization would come from two sources: $1.3 billion from public housing agencies opting to use their reserved development funds, and $500 million of recaptured development funds retained by HUD for public housing agencies who do not have funds to recapture.

PERMANENT FINANCING OF PUBLIC HOUSING

Prior to fiscal year 1980, the notes and bonds issued to finance public housing development and modernization were sold on the private market, and the investor yields from such obligations were not subject to federal taxation. Beginning in 1980, HUD initiated a program of selling such obligations to the Federal Financing Bank (FFB) to finance such purchases. The FFB borrows from the Treasury at an interest rate which reflects the yield paid by the Treasury on related taxable obligations which it sells. The FFB requires reimbursement from HUD for its borrowing cost--the difference between a "taxable" and "tax-exempt" interest rate. This is a "cash expenditure" in the HUD budget rather than a "tax forgiveness" to investors. No long-term bonds have been sold on the private market since 1974; public housing has been financed through "roll overs" of temporary loan notes; at the end of fiscal year 1981, outstanding public housing loan notes totaled $19.1 billion.

The 1982 and 1983 budgets provide for the use of $1.4 billion in budget authority in each year to cover the interest differential in sales of public housing obligations to the FFB.

TRIMMING THE PRODUCTION PIPELINE

In addition to strategies aimed at reducing existing federal obligations for assisted housing, both the 1982 and 1983 budgets propose trimming back federal commitments for projects in the assisted housing production pipeline. The total pipeline, from approved applications to projects under construction, is estimated at 700,000 units.

Of these, some 322,762 units have firm, contractual commitments: 160,092 Section 8 new construction/substantial rehabilitation units; 138,470 public housing units; and 24,200 Section 235 homeownership units. The HUD budget states that many of these projects (estimated at 145,000 units) are not financially viable, and anticipate that they will be cancelled. The HUD budgets for 1982 and 1983 anticipate that about 200,000 units in this firm pipeline will proceed to construction. Much of any success in moving to construction will depend on several factors, particularly if the interest rates on housing bonds are sufficiently low to make HUD's financial adjustment factors (FAF) work; and the availability of Section 8 tandem financing which is in short supply. Early June, 1982 deadlines affect both of these factors.

Difficult issues also revolve around the additional backlog of almost 400,000 units which have approved applications but no firm HUD commitments. Some of these projects are reaching the contract stage and the indication from HUD is that they will not be funded.

Chart I -- The Modified Section 8 Housing Certificate Program

(Subject to detailed authorizing legislation being drafted by HUD for submission to Congress)

Budget Commitment: The HUD 1983 budget includes $1.1 billion in budget authority to support 106,615 units under the new program--30,000 units to be used in conjunction with the newly-proposed rehabilitation grant program; 60,615 units involving conversion of units now under the Section 8 existing housing program; and 10,000 units to be used in conjunction with the sale of HUD-owned properties.

Term of Federal Authorization: The current Section 8 existing housing program has an authorization term of 15 years, with 5-year contract renewals. Budget authority is calculated without the inclusion of tenant rent contributions, permitting the establishment of a reserve fund to adjust family assistance in response to rent increases. The modified Section 8 program would provide budget authority only for a 5-year period, and only to cover actual family assistance payments calculated at the beginning of the lease term.

Maximum Rent Level: The current Section 8 existing housing program has a rent ceiling equal to a "Fair Market Rent" determined for the local area on the basis of the rental cost of units in the existing housing supply. Under the modified program, there would be a standard rent criterion, falling somewhat below the calculated "Fair Market Rent". This standard would not be a ceiling rent, but the base for federal assistance to the family; i.e., the federal government would provide assistance equal to the difference between 30 percent of a family's income and the rent standard. A family would be free to locate a unit with a rent either higher or lower than the standard: if higher, the family would pay the difference; if lower, the family would still keep the total federal assistance payment based on the standard. The average family assistance payment is calculated at about $2,000 per year.

Income Limits: Traditionally, the Section 8 existing housing program had an income eligibility ceiling of 80 percent of median income in the local area. Federal legislation in 1981 adjusted income limits for HUD-assisted housing to require that, on a national basis, only 10 percent of families in existing units would have incomes between 50 and 80 percent of median income; and only 5 percent of families in new units. The modified Section 8 program would restrict eligibility to families with incomes below 50 percent of median income on a local program basis.

Housing Quality Standards: Units to be leased would be inspected for minimum standards of health and safety. The local community could utilize standards of the local housing code, or utilize the current housing quality standards established by HUD.

Administrative Mechanisms: The modified Section 8 program would be administered, as the current Section 8 existing program is, by local public housing agencies and State agencies. However, it is anticipated that these administering agencies will take a smaller role than in the current program in such matters as outreach to families and to landlords, lease negotiations with the landlord, and evictions. The Administrative Fee would be reduced to correspond with a reduced role.

Chart II -- Proposed New Program of Rental Rehabilitation Grants

(Subject to detailed authorizing legislation being drafted by HUD for submission to Congress)

Budget Commitment: The HUD 1983 budget includes $150 million in budget authority to support a level of 30,000 units under a new rental rehabilitation grant focused on small rental properties at an average grant of $5,000 per unit. The federal grant could be used to finance not more than 50 percent of the cost of individual rehabilitation projects, with localities financing the other half ($5,000) The program is aimed at rehabilitating rental properties at competitive market rates for the neighborhoods in which they are located. This new program would replace the Section 312 rehabilitation loan and the Section 8 existing moderate rehabilitation programs.

Linkage with the Modified Section 8 Housing Certificate Program: The HUD 1983 budget earmarks $300 million in budget authority to support 30,000 units of the modified Section 8 housing certificate program to be used in conjunction with the rental rehabilitation grant program. This will support occupancy by lower income families in the rehabilitated units. (For a description of the modified Section 8 program, see Chart I)

Allocation of Federal Grants: A portion of the grants will be allocated by a needs formula to qualifying cities and towns with 50,000 or more in population, as well as to urban counties. Remaining funds will be allocated to interested state governments who will operate their own rehabilitation programs or will make funds available to other localities in the state.

Neighborhood Location Requirements: HUD grants will be eligible for use only in low and moderate income neighborhoods, as defined by HUD. The bulk of units are planned to be located in neighborhoods where market rents are low enough so that rehabilitated units will be affordable to modified Section 8 certificate holders without any need for rent controls. A HUD program standard will require that 80 percent of the rehabilitated units be affordable at market rates to certificate holders.

Rehabilitation Standards: All rehabilitated units must meet the HUD Housing Quality Standards utilized in the Section 8 existing housing program, except that localities may utilize their own housing or building codes to establish a program rehabilitation level which is higher than the HUD standards.

NAHRO Policy Analysis

TABLE 1. MAJOR ELEMENTS OF HUD BUDGET: FISCAL YEARS 1981, 1982 AND 1983

	Budget Authority (Dollars in Millions)			Budget Outlays (Dollars in Thousands)		
	1981 Actual	1982 Estimate	1983 Proposed	1981 Actual	1982 Estimate	1983 Proposed
Community Planning & Development						
Community Development Grants	$3,694.6	$3,456.0	$3,456.0	$4,042.4	$4,005.0	$3,350.0
Urban Development Action Grants	675.0	440.0	440.0	371.1	525.0	550.0
Planning Assistance (701)	---	---	---	38.9	20.3	4.7
Urban Renewal Closeouts	---	---	---	143.7	100.0	70.0
Rehabilitation Loans (312)	---	---	---	50.0	10.0	(-17.4)[2]
Urban Homesteading	---	---	12.0	(6.9)[1]	20.0	12.0
Rental Rehabilitation Grants (new)	---	---	150.0	---	---	---
Housing						
Section 8 & Public Housing	$24,983.0	$17,403.8	$24.8	$5,746.5	$6,726.0	$7,352.0
Rescission (including rent supplement)	-143.5	-12,187.3	-5,245.9	---	---	---
Net Available	$24,839.5	$ 5,216.5	-$5,221.1	$5,746.5	$6,726.0	$7,352.0
Operating Subsidies (public housing)	1,070.8[3]	1,292.9[4]	1,075.0	928.6	1,278.0	1,110.0
Flexible Subsidy (Troubled FHA Projects)	18.1	4.0	---	52.7	63.0	24.0
FHA Insurance Fund	412.1	251.5	134.2	181.5	-244.7	-1,178.7
Section 202 Housing for Elderly or Handicapped	797.0	744.5	276.6	917.4	711.0	286.3
Public Housing Loan Fund: Borrowing Authority	34.4	---	---	---	---	---
Housing Counseling	7.0	3.5	---	5.4	4.0	2.5
GNMA						
Section 8 & Targeted Tandem	$1,352.9	$1,249.4	---	$1,183.9	$1,009.9	$1,115.6
All Other						
New Communities	47.6	33.1	32.8	50.3	34.8	33.4
Research & Technology	39.7	20.0	20.0	43.2	27.7	25.5
Fair Housing	5.7	5.0	5.7	0.7	7.6	5.2
Other	356.0	303.0	303.5	367.1	294.9	366.5
TOTAL	$33,493.9	$25,207.1	$5,930.6	$14,033.4	$14,614.5	$13,129.9
NET TOTAL	$33,350.4	$13,019.8	$ 684.7	$14,033.4	$14,614.5	$13,129.9

(1) originally included in FHA Insurance Fund
(2) net receipts included within revolving fund (liquidating program)
(3) actual authority available after supplemental appropriation is $1102.6
(4) A total of $140.6 is allocated for FY1981 supplemental

Definitions:

Budget Authority -- means new or increased authorizations committing the Federal government to incur budget outlays. In the case of assistance for housing projects, total budget authority has traditionally been calculated for the full term of the commitment from 20 to 40 years.

Budget Outlays -- are annual expenditures made in payment of obligations incurred from budget authority.

TABLE 2. TERMINATION OF ACTIVITY: PROPOSED HUD BUDGET: FY1983

	Year Initiated	Dwelling Unit Reservations High Year	Dwelling Unit Reservations Actual FY1981
New Construction of Assisted Housing			
Section 8 (new construction and substantial rehabilitation)	1974	1977: reservations 169,396	73,861
Public Housing (new construction and acquisition)	1937	1969: ACCs 108,783	36,376
GNMA Tandem Assistance			
Regular Section 8 Tandem Targeted Tandem	1968	Purchase Authority: FY1981 $1,500,000,000 300,000,000	
Section 8 Moderate Rehabilitation	1979	Dwelling Unit Reservations (FY81) cumulative: 118,184	
Housing Counseling Grants	1968	Budget Authority: FY1981 $10,000,000; counseling agencies funded: 212	
Section 701 Comprehensive Planning Grants	1954	Budget Authority: FY1981 $33,750,000	
Section 312 Rehabilitation Loans	1964	Budget Authority: FY1981 $129,980,000; cumulative loan reservations: 88,602	
Neighborhood Self-Help Development Grants	1978 Terminated: 1981	Budget Authority: FY1981 $9,000,000; cumulative grants: 125	
Section 108 (CDBG Loan Guarantees)	1974	Loan Authority Available: 1982 Ceiling: $225,000,000 # of Commitments, 1981: 42	
Solar Energy and Conservation Bank	1980: To be terminated prior to start up	Budget Authority: FY1981 $125,000,000	

TABLE 3 -- AVAILABILITY AND UTILIZATION OF BUDGET AUTHORITY FOR SECTION 8 AND PUBLIC HOUSING: FISCAL YEAR 1982 ($000)

Availability of Budget Authority		
Carry-over from previous year	$2,772,058	
Available for re-use	30,257	
New authorization	17,373,528	
Authority to be recaptured	7,483,845	
Total	$27,659,688	
Authority to be Rescinded	$ 9,399,789	34%
Summary of Utilization of Net Authority (After Rescissions)		
1. New activity: New construction, substantial rehabilitation, acquisition of existing housing	$ 2,956,020	16%
2. Amendments to new activity in process or under construction	$ 3,606,800	20%
3. Conversion or disposition of assisted housing projects	$ 7,849,200	43%
4. Payments for FHA-insured troubled projects	$ 202,500	1%
5. Section 8 support of existing private units (conversions and adjustments)	$ 445,379	2%
6. Modernization of public housing	$ 1,800,000	10%
7. Sale of public housing obligations to Federal Financing Bank (interest differential payments)	$ 1,400,000	8%
Total	$18,259,899	100%

BEST DOCUMENT AVAILABLE

TABLE 3-4 -- DETAILED ANALYSIS OF UTILIZATION OF NET BUDGET AUTHORITY AFTER RESCISSION

FY1982

($000)

Use	Budget Authority	Dwelling Units
1. New activity: New construction, substantial rehabilitation, acquisition of existing housing.		
--Section 8 set aside for Section 202 elderly or handicapped housing	$2,099,692	16,933
--Section 8 new construction/ substantial rehabilitation	806,948	5,272
--Public and Indian housing (including acquisitions)	49,380	310
Total	$2,956,020	22,515 units
2. Amendments for Section 8 and public housing in processing or under construction	$3,606,300	not available
3. Conversion or disposition of existing assisted housing projects		
--Conversion of rent supplement and Section 236 rental assistance payment projects to Section 8-leasing assistance	$7,162,200	Rent supplement units: (160,000 + 13,000 Section 236 units) (60,000, 1982) (60,000, 1983) (40,000, 1984)
--Use of Section 8 assistance for disposition of units in HUD-owned multi-family projects	687,700	10,000
Total	$7,849,200	183,000
4. Payments for FHA-insured troubled projects	$ 202,500	5,000

5. Section 8 support for existing housing units: conversion and adjustments		
--Conversion of Section 23 units to Section 8	$ 188,325	5,000
--Assistance to families residing in Section 8 new construction if owner does not renew 5-year contract	54,000	1,000
--Lease adjustments to Section 23 units	24,800	not available
--Other adjustments	178,254	not available
Total	$ 445,379	6,000 units
6. Modernization of public housing	$1,800,000	estimated to finance $981.9 million of capital improvements
7. Sale of public housing obligations to Federal Financing Bank (interest differential payments)	$1,400,000	estimated sales of $1.026 million of obligations in FY 1983
Total	$18,259,899	216,515 units (where applicable)

BEST DOCUMENT AVAILABLE

TABLE 4 -- AVAILABILITY AND UTILIZATION OF BUDGET AUTHORITY FOR SECTION 8 AND PUBLIC HOUSING: FISCAL YEAR 1983

Availability of Budget Authority		
Available for re-use	$ 24,800	
Authority to be recaptured	9,919,137	
Total	$9,943,937	
Authority to be Rescinded	$2,415,541	24%
Summary of Utilization of Net Authority (After Rescissions)		
1. New activity: New construction, substantial rehabilitation	$1,310,000	17%
2. Amendments to new activity in process or under construction	$1,700,000	23%
3. Section 8 support of existing private units (conversion or adjustments)	$ 227,125	3%
4. New program of modified Section 8 certificates (including administrative costs)	$1,091,271	14%
5. Modernization of public housing	$1,800,000	24%
6. Sales of public housing obligations to Federal Financing Bank (interest differential payments)	$1,400,000	19%
Total	$7,528,396	100%

TABLE 4-A -- DETAILED ANALYSIS OF UTILIZATION OF NET BUDGET AUTHORITY AFTER RESCISSION

FY1983

Use	Budget Authority	Dwelling Units
1. New activity: New construction or substantial rehabilitation		
--Section 8 set-aside for the Section 202 program for elderly or handicapped housing	$1,310,000	10,000
2. Amendments for Section 8 and public housing in processing or under construction	$1,700,000	not available
3. Support of existing private housing units		
--Conversion of Section 23 units to Section 8 existing housing	$ 203,325	5,000
--Adjustments to Section 23 units under lease	$ 23,800	not available
4. New program of modified Section 8 certificates		
--Administrative costs	$ 25,121	---
--Units to be leased:		
Conversion of units now under Section 8 existing program	$ 606,150	60,615
Support of units under new rental rehabilitation grant program	$ 300,000	30,000
--Support of units in conjunction with the sale of HUD-held properties	$ 100,000	10,000
--Support of residents of public housing where units are sold or demolished	$ 50,000	5,000
--Assistance to families residing in Section 8 new construction if owner does not renew 5-year contract	$ 10,000	1,000
Total	$1,091,2[illegible]	106,6[illegible]5

BEST DOCUMENT AVAILABLE

5. Modernization of public housing	$1,800,000	estimated to finance $931.9 million of capital costs
6. Sales of public housing obligations to Federal Financing Bank (interest differential payments)	$1,400,000	estimated sales of $1.425 million of obligation in FY1984
Total	$7,528,396	121,615 (where applicable)

NAHRO COMMENTS ON THE ADMINISTRATION'S PROPOSALS

Modified Section 8 Certificates

The Section 8 program, as currently constituted, is a successful and effective program; the proposed changes, we believe, could have an adverse effect on the interest of the family, the landlord, and the administering agency. We support the continued requirement that units under this program must meet Housing Quality Standards. Beyond that, our concerns about the changes being proposed to the Section 8 existing housing program are as follows.

- Income Limits. The proposal to limit eligibility to families with incomes 50 percent of the area median income or below has problems. It eliminates from eligibility the "working family" with children, whose income falls between 50 percent and 80 percent of median income, and whose housing needs are at least as critical as those of non-working households with lower dollar incomes. Professor Michael Stegman of the University of North Carolina has documented this situation in an article in the December, 1981, issue of the *Journal of Housing*; we respectfully request that this article be included in the hearing record. Based on analysis in New York City, Professor Stegman found that Section 8 program participants with incomes between 50 and 80 percent of the median income were:

  --disproportionately minority (66 percent were black and 15 percent Hispanic)

  --more likely to be households with children (52 percent are one-parent households with children and 25 percent are households with two parents and children)

To deny such families eligibility for a Section 8 certificate would be to deny assistance to families with critical housing needs.

- Payment Standards. The modified certificate program establishes a new "standard" at a point below the currently-calculated Fair Market Rents, to govern federal assistance payments. This standard would be determined by the Secretary of HUD without any opportunity for public comment; he has indicated his intention to establish such a standard at 80 percent of the current Fair Market Rents. Federal assistance would be the difference between this "standard" rent and family rent payments based on 30 percent of adjusted family income; there would also be a minimum rent requirement. A family would be free to pay more or less than the "standard" rent; if more, the family would absorb the additional cost; if less, it would keep any difference. Also, the initially-calculated assistance to the family would be set for the term of the lease, even if the family moved to other housing. There would be no adjustment in the event of rent increases.

This new "rent standard" policy would have serious impacts on the low-income family. While the justification is that it will give the family more freedom of choice in its housing, it could well result in a family stretching beyond its means for the only available standard housing in the local market; and having to absorb any increases in rent. NAHRO believes that the current Section 8 existing program and the Fair Market Rent system is a better way to assure equity for the family. While we recognize that not all assistance should gravitate to the level of the Fair Market Rent, we believe there are other remedies than the one proposed. One solution is to provide further leeway for the public agencies to negotiate rents with landlords; another is to refine the documentation for setting rent levels for standard, available housing in the community.

- Role of the Administering Agency. While it is not spelled out in the proposed legislation, the discussion surrounding its introduction indicates a desire for maximum "freedom" between the "family" and the "landlord" to implement a certificate program. This could result in administrative regulations which would deny families the assistance of the public agencies in locating housing, in overseeing the lease document, and in monitoring the family-landlord relationship over the lease term. Experience under the existing program indicates that there are important safeguards in the program for both the family and the landlord. We would caution against their elimination.
- Attractiveness to Landlords. Several proposed provisions of the new modified certificate program could significantly affect landlord interest in participating in the program. First, the reduced level of assistance payments based on the payment standard, and the "fixed" nature of this payment during the lease term, could raise questions about the family's ability to meet its rent obligations. Secondly, the provision (Section 202 a-5) which states that "no assistance payment shall be made for any unit after the month during which the unit was vacated" removes the security for the landlord currently provided in Section 8 (c)(4), which provides payment for up to 60 days after the unit is vacated. Finally, any reduction in the role of the administering public agency as described above, removes assistance available to resolve any problem areas in implementing the lease arrangement.
- Method of Budget Calculation. Another serious problem with the new proposal, from our viewpoint, is the change in method of federal funding in the HUD budget. Under the current system, budget authority for the Section 8 existing program is committed for the full term of the leases, not including the family rent contribution. This makes

possible the establishment of a reserve fund to take care of additional family assistance if rents should be increased. There is no such provision in the new proposal. Elimination of the reserve fund would not only work to the detriment of the family, but would also remove a basic factor in the stability and efficiency of the program.

Rental Rehabilitation Grants

Inasmuch as the rental rehabilitation initiatives proposal is based on a desirable objective--to help preserve the nation's rental housing stock in low and moderate income neighborhoods--NAHRO is pleased at the Administration's recognition of this need. We strongly feel, however, that the crisis in housing that our nation now faces will be little served by this program. New construction initiatives should be a much higher priority on our housing agenda--we have existing workable programs for rehabilitation whose major drawback these days is underfunding. The use of funds proposed for this rental rehabilitation grant should best be left to local determination in existing CDBG rehabilitation efforts. As described, this program would restrict local flexibility in designing rehabilitation programs which most economically suit local needs by forcing localities to come up with up to one-half of the costs of financing these units. We believe that the proposed new program gives too little and asks too much. It should in no case be considered as a major component of any housing bill.

Additional Comment

It is apparent that certain of the Administration's proposals are being made without considering the combined impact on both the income of the tenants and the operating income available to assisted housing programs. These legislative proposals threaten the stability of the programs and particularly our ability to house low income persons. They are made at a time when cut-backs are being made in employment programs, health care, nutrition and social services, and against a backdrop of unemployment which is at a 40-year high in many parts of the country.

The Administration's new proposals we refer to include:

- including food stamps as income in determining rent levels in housing programs;
- considering the value of housing assistance in computing levels of welfare assistance;
- eliminating all deduction from income in calculating rents; and
- modifying last year's legislation to permit rent increases of up to 20% per year.

Michael A. Stegman

Housing vouchers: recommendations of the President's Commission on Housing

During the final 18 months of the Carter Administration, a five-year research phase of HUD's experimental housing allowance program was completed. Policy debates and discussions at that time sometimes raised such existential questions as whether any HUD effort that reduced relative housing expense burdens so much while contributing nothing to new supply and so little to improved housing quality had the right to be called a housing program.

There also occurred attempts, none of which materialized, to develop joint HUD HHS initiatives to improve the housing situations of families receiving public assistance — particularly those receiving Aid to Families with Dependent Children who, despite their shelter allowances, continue to occupy inadequate housing at exceptionally high rates. A number of supply-side demonstrations, some of a self-help character in deteriorated inner-city neighborhoods and others in equally distressed but quite different markets in poor, sparsely settled rural communities across the country were under way. These efforts were either of a neighborhood rebuilding or stabilization character or were intended to encourage the private market to respond to rural needs by increasing the accessibility of existing mortgage insurance and other public programs to market actors in rural communities.

These occurrences are meaningful in light of five issues that relate to the recently released *Interim Report of the President's Commission on Housing* and its call for a program of consumer-oriented housing assistance grants. The issues are:

1—the importance of housing standards and the consequences of a transfer of a successful voucher program from HUD to the Department of Health and Human Services;

2—what EHAP does not tell us about the costs and optimal role of vouchers in a national low-income housing policy;

3—the adequacy of "supply" in urban and rural areas;

4—income eligibility and aiding the most needy poor; and

5—vouchers as a replacement for public housing subsidies.

Housing Quality Standards

The Commission expressed the view that, whatever size a voucher program might take, ". . . because the objective of national housing policy is a decent home for every American family, recipients of housing assistance grants should be required to occupy standard housing." A major concern, however, is the intent of of the Administration to get HUD out of the housing

Dr. Stegman is Professor of City and Regional Planning, University of North Carolina at Chapel Hill, and former Deputy Assistant Secretary of Research, Department of Housing and Urban Development, Washington, D.C.

business and the implications of such an eventuality in terms of the maintenance of housing quality standards in a voucher program. In a recent speech to the National Association of Realtors in Miami Beach, HUD Secretary Samuel Pierce underscored the Reagan Administration's commitment to get ". . . out of the business of building housing for low- and moderate-income families, and to use tax incentives to stimulate private investment in urban areas." Whether one favors this policy thrust is not the point. What is important is that, with the loss of its direct low-income housing production responsibilities, HUD will, *de facto*, if not *de jure*, relinquish its leadership role in the low-income housing area. The voucher function will be transferred to the Department of Health and Human Services and integrated into a public assistance block grant. The housing quality standards associated with housing vouchers surely will vanish.

> *"How in the world can housing authorities improve their competitive positions relative to private housing suppliers when the local authorities' financial condition is now being seriously undermined...?"*

During the latter part of the Carter Administration, several state welfare directors proposed demonstrations that would link public assistance to HUD's Section 8 housing quality standards, incentives, and procedures for encouraging landlords housing welfare families to maintain their units at minimum levels of adequacy. These officials had been frustrated in their efforts to develop enforceable housing quality requirements wholly within their programs. Law, tradition, and the substantial ideological opposition that exists within the welfare establishment to earmarking and restricting the rights of public assistance clients to manage their cash assistance payments as they see fit—which could be necessary in some welfare-housing initiatives—hindered those efforts. Also, welfare shelter allowances frequently are inadequate to pay for decent housing. The linking of Section 8 to public assistance was viewed as a way of expanding welfare resources through a housing set-aside. In New York City, for example, the Section 8 fair market rent for an existing two-bedroom unit is at least half-again as high as the shelter allocation for a family of four in the public assistance program.

From a budgetary standpoint, a voucher program with a minimum housing requirement would probably be no more resistant to budget cutbacks than would one without such a requirement. The presence of minimum housing standards in a voucher program, however, probably could alter the way in which budget cuts are absorbed within the program. Holding constant the percent of income a tenant must contribute to the payment of rent, the size of a housing allowance payment is a function of the cost of housing that just meets the quality standard for the local market. Once the required tenant rent contribution is raised to its highest practical level, budget cuts probably would be absorbed by reducing the number of households receiving assistance; any reduction in voucher payments per participant would put the cost of standard housing beyond the program clients' reach.

Without a housing quality standard to peg the minimum size of the needed housing allowance payment, it is more likely that the response to significant program cutbacks would be the reduction of the average household subsidy, rather than a reduced number of program participants. If this occurs, even the modest housing impacts of a voucher program would disappear altogether.

Program Costs—A Misleading Issue

Many students of housing hold in high regard the quality of HUD's experimental housing allowance research and the policy significance of its findings. Because of EHAP, a great deal is known about housing consumption and mobility patterns of households that are potential beneficiaries of a voucher program. EHAP has generated solid data on likely participation rates among household groups in an entitlement program. The supply experiments also have produced empirical estimates of rent inflation rates in local markets (which are negligible) and the effects of allowances on housing conditions and the size of the supply, both of which also are quite limited.

Indeed, in the past, based on these and related EHAP findings, HUD's office of policy development and research unsuccessfully proposed modifications to the Section 8 existing housing program similar to some of those now being endorsed by the President's Commission and OMB. Among these proposed modifications were making Section 8 payments directly to tenants, rather than to landlords, and removing the FMR limit as a condition of occupancy while maintaining it as a basis for determining the actual subsidy a family receives. This latter modification means that a family wishing to occupy a dwelling that rents higher than the FMR would have to pay the full amount of the difference out of its own funds while any savings due to occupancy of a unit that rents below FMR would likewise be kept by the family. These changes would open up the housing stock available to participants and would have a dampening effect on program-induced rent inflation.

In discussing vouchers, it is important to distinguish between these and related policy implications that are directly related to EHAP and those that are misleadingly cloaked in EHAP. For example, while EHAP has produced very good estimates of the unit cost of assistance in an allowance program, the experiments reveal precious little about an optimal housing program mix or the extent to which national housing policy ought to be dominated by demand side programs. The President's Commission correctly indicates that "A basic equity problem of all subsidized housing is that relatively few obtain program benefits from among the eligible population." The fact that housing allowances cost about half as much as supply-side subsidies means that "Twice as many households can be served at any given level of funding under the consumer-oriented programs as under the construction programs." Despite implications to the contrary, the Commission knows that the Administration has no intention of using the cost advantage of housing vouchers to expand dramatically the fractions of the eligible population that would receive housing assistance under a voucher-type program and thereby lessen the equity problem inherent in supply-side programs. A much more likely scenario is one in which housing vouchers would replace housing development under existing supply programs, with the savings in contract and budget authority being extracted from the housing sector through recissions or reductions in future appropriations.

With respect to the issue of the higher unit cost of supply side programs, the Commission and the Administration point out that the so-called budget overhang of subsidized housing programs is so enormous that production efforts must be sharply curtailed. Outstanding obligations associated with the Section 8 new construction program alone amount to $110 billion and already extend a generation into the future. The total unpaid bill for all low-income housing constructed since the federal government got into the assisted housing business 40 years ago now totals $250 billion.

Budget data are no more informative nor instructive of a particular housing policy course than are similar kinds of data concerning the size of the tax expenditure budget for owner-occupied housing. The cost in terms of foregone federal taxes of just the mortgage interest deduction for home owners for the five years between 1982 and 1986 will be nearly twice the size of the entire 40-year, Section 8 budget overhang. That a cap on mortgage interest deductions and the conversion of the deduction to a tax credit could possibly save the government enough money to maintain an adequate level of low-income housing production, follows no more directly from the data on the size of the mortgage interest subsidy to non-lower-income home owners than does a policy of housing vouchers follow directly from data on the cumulative obligations associated with deep subsidy production programs.

The fact is that all the cost advantages of housing allowances really reveal is that whenever and wherever possible housing vouchers should first be considered as the principal housing assistance tool before resorting to supply-side efforts. Few would argue with this proposition. The important question is the extent and conditions under which, despite their higher unit costs, supply side programs may be necessary or desirable to achieve important local and national housing policy objectives; and whether local housing supplies are adequate to accommodate the housing needs of lower-income families.

Housing Adequacy

An important part of the policy debate on housing vouchers hinges on the adequacy—not of the nation's housing supply—but of thousands of local housing supplies to serve the needs of lower-income families, including those now living in physically adequate housing and those now occupying substandard dwellings. To the extent that the former have an excess rent burden, they could receive housing allowances in place. The latter would have to have their present units upgraded or would have to move to acceptable housing in order to receive rental assistance. The experimental housing allowance program indicates that upgrading is likely to occur as a result of housing allowances only if the needed repairs are very modest. Program incentives are just too small to encourage any real degree of rehabilitation and capital investment.

Here, the lessons of EHAP are instructive, but not decisive, in terms of national housing policy. The experiments demonstrated that while allowances have virtually no effects on the size of supply—in the experimental sites, at least—much of the existing stock responded well to program demands, and proved capable of being upgraded to minimum program standards at a per dwelling investment of no more than a year's cost of cigarettes for a light smoker. This, however, does not mean that the supply of available housing in all kinds of communities across the country is equal to the housing voucher task.

The designers of the allowance experiments acknowledge that their statistical findings should not be generalized. They do, however, argue correctly that the stability of important housing market outcomes across diverse pairs of supply and demand sites suggests that the findings are likely to be applicable to a cross section of communities far larger than the four experimental sites of Pittsburgh, Phoenix, South Bend, and Green Bay. Nevertheless, they stop short of suggesting that the national housing scene is no different than the EHAP picture "writ large."

Though somewhat reluctantly, the President's Commission acknowledges this fact. After emphasizing that the most serious national housing problem today is one of affordability and not housing adequacy, the Commission recognizes the existence of ". . . some geographic concentrations of inadequate units."

"They are found," says the Commission, "disproportionately in rural areas in the South and in older large cities. New York City and the nearby New Jersey cities of Newark, Paterson and Jersey City showed a particularly high concentration (19 percent), double the average of other large cities. Inadequate housing," noted the Commission, "also is more frequently found among certain types of households. Minority households—particularly black households—occupy such housing much more often than non-minority households. Female-headed households and the elderly also have above-average incidence of housing inadequacy."

When these bland acknowledgements are translated into housing conditions at the local level, their impact becomes more real. In New York City, for example, the results of a special housing and vacancy survey by the Bureau of the Census of the city's rental housing market shows very high levels of housing inadequacy among the above noted population groups. Using data on maintenance and equipment deficiencies similar to those used by the Congressional Budget Office and the President's Commission to identify housing in need of rehabilitation, this 1981 census survey indicates that:

—35 percent of all black and 38 percent of all Puerto Rican renter households occupy housing in need of rehabilitation;

—34 percent of all renter households containing five or more persons are inadequately housed, as are one-quarter of all female-headed renter households; and

—47 percent of all renter families receiving public assistance live in housing needing rehabilitation.

Indeed, spending a high proportion of one's income on rent does not guarantee occupancy of adequate housing in New York City. Nearly one-third of all households spending at least 40 percent of their incomes for rent also occupy inadequate housing.

Rather than concluding from its assessment of the inadequate supply problem that supply-side programs should be made more cost-effective and targeted to the areas most in need, the Commission proposes, essentially, that the government end these programs and open up the community development block grants to include low-income new construction. With large cities already struggling to cope with previous cutbacks in community development block grants, threatened with the loss of UDAG, and now fighting to fend off OMB's proposal to zero out block grants after fiscal year 1984, the Commission's proposal can be scarcely viewed as a responsible policy position. This is, of course, true not only in the case of large older cities. It is equally true for many rural communities, many of which have staggering concentrations of inadequate housing. In the state of North Carolina, for example, at least 20 percent of the rental stock in one fifth of the state's counties lacks complete plumbing for the exclusive use of its occupants. Many of these and other rural communities throughout the country have no certainty of receiving small cities CDBG funds, and little or no competence to develop and finance low-income housing without substantial technical support. Further, states preparing to assume administration of the program will now be less willing to provide that assistance in light of OMB's plans to phase out the program a few years from now.

What might inadequate supply mean to a housing voucher program? Having seen the housing statistics for New York City, a group of researchers from Pratt Institute in New York analyzed the city's Section 8 existing housing program to determine whether the high incidence of housing problems has made it difficult for various household groups to participate in this voucher-like program.

In their draft report now under review, the Pratt researchers found that 27 percent of the households that were issued Section 8 certificates between January 1979 and May 1981 never became recipients of any rental housing assistance. Households that either wanted to or who were required to move to receive Section 8 assistance were substantially more likely to become program dropouts than were households that wanted or were able to receive the subsidy in place. More than one half of the certificate holders who wanted to or had to move never received any assistance compared to only 15 percent of the certificate holders who were eligible to remain in place.

The families with certificates that wanted to or had to move in order to receive Section 8 comprised 56 percent of all non-elderly singles, 71 percent of all families with children, 63 percent of all non-elderly couples, but only 40 percent of all elderly singles and couples. Because of the difficulty of finding suitable housing in a tight New York City rental market that had a 1981 net vacancy rate of just 2.1 percent, 50 percent of all two parent families with children became Section 8 program dropouts. Fifty-one percent of all non-elderly couples never became recipients. Only 15 percent of all elderly couples and 30 percent of all elderly singles with certificates failed to receive Section 8 payments.

Defining the Eligible Population

As a basis for allocating scarce housing resources, the Commission properly argues that assistance should be targeted to those most in need. One might concur with the operational definition of the urgent needs population, namely, households whose incomes are very low, no higher than 50 percent of the area median. Nationally, the Commission points out, the incidence of housing inadequacy among very low-income renters is twice as great as among low-income renters—20 percent, compared to slightly more than 10 percent.

This is not necessarily the case among Section 8 existing housing program participants in New York

City, where important differences exist between very low-income and low-income households. Should these differences be repeated elsewhere in the country, the very low-income program eligibility criterion could have unintended and undesirable screening effects.

According to the Pratt Institute researchers, very low-income Section 8 recipients tended to have the following characeristics:

—a majority are white (58 percent),

—a majority are elderly (60 percent),

—a small minority (22 percent) had children in the household, and

—only slightly more than one-third wanted to or were required to move to receive Section 8 benefits.

In stark contrast, the researchers found low-income program participants, those with incomes between 50 and 80 percent of the area median, to be:

—disproportionately minority (66 percent were black and 15 percent hispanic);

—more likely to be households with children (52 percent are one parent households with children and 25 percent are households with two parents and children), and

—likely to have to move in order to qualify for Section 8 assistance (73 percent of low-income Section 8 recipients fell into this category).

In short, it is not that clear that the degree and urgency of housing need among poor people is simply a function of just how poor they are.

Despite agreement with the Commission's view that a larger part of the low-income housing program burden can be properly, responsibly, and effectively shouldered by a demand-side program, one concludes a reading of its Interim Report feeling very ill at ease. A significant amount of discomfort comes not from the Commission's work itself but from concern over how its analysis and recommendations will be interpreted and used by an Administration that is generally unsympathetic to the housing needs of poor people.

A good example can be illustrated in the potential relationship between housing vouchers and public housing subsidies. Under certain conditions, among them being the elimination of serious problems of deferred maintenance and the improvement of the energy efficiency of the public housing inventory, one could support the Commission's goal of having consumer oriented housing assistance grants eventually replace public housing operating subsidies. The theory is that if local housing authorities cannot successfully compete in the open low-income market place for voucher-enhanced low-income consumers' housing dollars, then perhaps they should get out of the business. The practical dangers of embracing this goal, however, are two-fold. First, the Commission proposes that the budget authority associated with vouchers should be limited to between three and five years. This means that local public housing authorities would soon find themselves with tenants who will be unable to pay their rents three years down the road, a condition in the private rental housing market that leads investors to adopt very short run investment strategies of undermaintenance and eventual abandonment. Second, and more important, while it is a good intellectual exercise to theorize about the outcomes of the competitive interactions of unfettered public and private housing suppliers as they vie for the low-income housing dollar, in the present budgetary environment, this theorizing is no more than that—an intellectual exercise.

How in the world can housing authorities improve their competitive positions relative to private housing suppliers when the local authorities' financial condition is now being seriously undermined by the Administration's callous disregard for their demonstrated needs for continued operating subsidies? Each day brings either another release or news leak that reads like a weather report during a cold snap. A short time ago, the weather was mild, the breezes balmy and housing authorities were going to be funded at a level of 82 percent of demonstrated need. Then, the clouds rolled in and the "temperature" dipped to 75 percent and, according to some, the true operating subsidy reading was just 69 percent in the shade. In the first week of December, the storm clouds gathered, the sky darkened, and OMB's forecast was for a fiscal year 1983 operating subsidy level of a frigid 25 percent of true need.

The irony of all this, of course, is that the Administration seems intent on destroying the public housing system that the President's Commission wants to see become more market-oriented and competitive in the future. If OMB's plan is adopted, the outcome of the market test will be very predictable and the Administration's anticipation of the failures of the public housing system will become a self-fulfilling prophecy.

In their increasingly debilitated states, housing authorities will be unable to compete successfully for the voucher-enhanced consumers' housing dollar. The most upwardly mobile families will leave public housing first, followed by others who are able to navigate in the local market. Enough tenants would leave their assisted units to assure the financial failure of many projects and local authorities. Not all projects would empty out, however, because local housing supplies will be unable to respond to the increased demand. As local projects deteriorate still further, they will become centers of frustration, tension, and unrest. More families will flee public housing, doubling up will increase in some cities, and private market rents would rise. Because the voucher program puts no cap on allowable rents and only a small portion of eligibles would be receiving rental housing assistance, more and more poor people would have to pay very high fractions of their incomes for inadequate housing. And toward what end? Merely to test the Commission's theory of housing market competition among private and public housing suppliers. The cards in the deck were stacked by OMB from the beginning.

BEST DOCUMENT AVAILABLE

NAHRO
Serving the Nation's Housing and
Community Development Needs

SUMMARY OF CDBG/UDAG QUESTIONNAIRE RESPONSES

The National Association of Counties (NACO), the National Association of Housing and Redevelopment Officials (NAHRO), the National League of Cities (NLC) and the United States Conference of Mayors (USCM) conducted a joint survey in February and March, 1982, of cities and counties to assess the local impact of funding cuts on the CDBG and UDAG programs.

The survey primarily covered the need for and impact of the major CDBG program activities--public works, housing and public services. Questions were raised as to the abandonment or delay of planned projects and shifts of project needs. Localities were asked to give examples of successful and significant projects funded under CDBD and UDAG programs and to include other funding sources for any on-going or planned projects that would fall through as a result of cutbacks in these programs.

Seventy-five (75) entitlement communities responded to the survey. Data from the CDBG/UDAG survey returns indicate several negative impacts of reductions in program funds. Planned projects have been abandoned; jobs have been lost and local revenues are expected to be impacted.

The most devastating impact on cities and counties will be if the Administration's proposed rescission of assisted housing units are passed by Congress. Communities surveyed have nearly 24,000 housing units that they are committed to provide as a result of planned activities, urban renewal plans, court settlements or HUD directives, such as performance reviews. These communities have committed CDBG, UDAG, or Section 108 loan guarantee funds toward this effort. Since this survey only reflects one-tenth of the total number of eligible entitlement communities, the total amount of funds already invested in expectation of receiving assisted housing funds could well be in the range of millions of dollars. These seventy-five communities have committed a total of $110 million in CDBG funds for various housing related activities in anticipation of receiving assisted huusing funds from HUD.

Highlights from the survey are described below:

o Overall Program - NATIONAL OBJECTIVES
The most frequent (over 90%) response to which national objectives are specified by local CDBG programs was clearly the conservation and expansion of the nation's housing stock.
The second and third most frequent (over 60%) responses were elimination of slums and blight and alleviation of physical and economic distress through the stimulation of private investment and community revitilization.

About one-third of the respondents felt that their local objective of conserving and expanding the nation's housing stock would change because of funding decreases.

- Public Works -
  The three most frequently cited public works activities were to provide curbs and gutters, street repair and storm drainage. These activities were most often used to improve residential neighborhoods, improve public health or safety and improve commercial strips and retain existing businesses.

  The most important impact these activities had which were cited by respondents include stabilized neighborhoods, visual improvements, increased property values and increased business activities.

  Over 85%of funds expended on thse public work activities were estimated to have benefitted low and moderate income persons.

- Housing -
  Over 80% of the respondents funded housing rehabilitation programs for owner occupants. More than 41,000 such units have been rehabilitated.

  Over 50% of the respondents funded housing rehabilitation programs for rental properties. About 13,500 such units have been rehabilitated.

  Almost half of the respondents had other types of housing programs such as home ownership assistance programs.

  About 60% of the respondents used private investments to leverage funds to provide financing. This ratio varies.

  Almost all housing programs have been used to bring property up to local codes and standards.

  Over 90%of the local housing programs have been used to improve energy conservation.

  Respondents estimated that over 15,000 homes were privately rehabbed because there was local CDBG rehabilitation taking place in a neighborhood.

  The most frequently cited impact of the rehabilitation programs has been to stabilize neighborhoods. Other frequent impacts have been to increase property values, to improve energy conservation, to make public health and safety improvements and to improve overall neighborhood appearance.

  Over 93% of the funds expanded on housing activities were estimated to have benefitted low and moderate income persons.

- Public Services
  The most frequent public service activities have been buildings for special purposes. These include such special use as senior centers, battered women shelters, day care centers and emergency shelters.

  An overwhelming majority (over 80%) of the respondents think that the reduction in other federally funded social and public services will put political pressure on funds.

  20% of the respondents thought that social and public services will will likely be funded out of CDBG at the expense of other activities.

- Other Activities
  Over 70% of the respondents use CDBG funds for other significant community activities such as commercial rehabilitation and other economic development activities.

- Impact of Funding Reductions
  Over half of the respondents have had to slow down work on on-going projects.

  About half of the communities responding have abandoned planned projects -- including activities such as street drainage plans, assembling and clearing land, rehabilitating abandoned buildings.

Existing obligations

The 75 communities have committed a total of $110 million in CDBG funds for various housing-related activities in anticipation of receiving assisted housing funds from HUD. Specifically, these communities have committed $45 million for land acquistion, $15.6 million for site clearance, $3.2 million to purchase buildings for rehabilitation, $17.4 million for site improvements, $11.7 million for plans and specifications, $700,000 in anticipation of low-interest bonds becoming available for Sec. 8 and $16.5 million for other related activities.

Many cities are obligated to provide new or substantially rehabilitated assisted housing units as a result of planned activities such as urban renewal plans, court settlements or HUD directives and have committed CDBG, UDAG or Sec. 108 loan guarantee funds toward this effort, on the expectation of receiving assisted housing units from HUD. If proposed rescissions of assisted housing units are passed by Congress, the communities will not be able to proceed with nearly 24,000 units that were planned as part of their CD programs.

Estimates for future funding needs

While not all respondents were able to make estimates of future funding needs, the response received indicated a far greater need than is available for funding. Out of 35 responses, the estimates for 1 year funding needs was as follows:

Funding needs for 1 year:

Public Works	$ 2.2 billion
Public Services	$ 2.8 billion
Housing	$ 1.1 billion
Units	240,000

Specific information on cities responding may be obtained from the representatives of the participating organ izations.

USCM	Barry Zigas	(202) 292-7330
NLC	Reggie Todd	(202) 626-3020
NAHRO	Sheryl Lincoln	(202) 333-2020
NACO	John Murphy	(202) 393-6226

CDBG/UDAG QUESTIONNAIRE

Jurisdiction____________________ Date____________

Congressional Representatives____________________

Population________________

Amount of FY81 Entitlement________________

Amount of FY82 Entitlement________________

1. OVERALL PROGRAM

Which of the following national objectives does your local CDBG program specify? (Check no more than three)

_____a. elimination of slums and blight

_____b. elimination of conditions that are detrimental to health, safety and public welfare

_____c. conservation and expansion of nation's housing stock

_____d. expansion and improvement of quantity and quality of community services

_____e. more rational utilization of land and other natural resources

_____f. reduction of isolation of income groups

_____g. restoration and preservation of properties for historic, architectural, or esthetic reasons

_____h. alleviation of physical and economic distress through the stimulation of private investment and community revitalization

_____i. conservation and expansion of the nation's scarce energy resources

Indicate by letter(s) which objectives will change due to funding decreases?

____

Will any of these objectives change due to revised regulations (as to be changed according to latest HUD notices)? Please specify.

2. PROGRAM ACTIVITIES

Public Works

Check which public works activities CDBG funds have been used for in your community.

Street repair________________

Sewer construction____________

Sewer reconstruction__________

Water line construction_______

Storm drainage_________

Water line reconstruction______________

Street lighting________________________

Curbs & gutters________________________

Other infrastructure or public works activities (please specify)____________________

Number the following in order of their impact: (Check as many as apply to the activities listed above)

These public works activities were needed to:

__________create jobs

__________retain jobs

__________attract new business(es)

__________retain existing business(es)

__________conserve energy

__________public health or safety

__________improve residential neighborhoods

__________improve commercial strips

__________other (please specify)__________

____

Check the following impact these projects have had (check as many as apply):

These public works activities have had the following impact in our city:

__________increased property values

__________helped stabilize neighborhoods

__________visual improvement

__________increased local taxes

__________increased job opportunities

__________increased business activity

__________other (please specify)__________

____

What percentage of funds expended on these public works projects have benefited low and moderate income persons?__________

Housing

Check the type of rehabilitation housing programs CDBG finances. Please indicate how many units have been rehabilitated:

__________Housing rehabilitation, owner occupants __________# of units rehabbed

__________Housing rehabilitation, rental __________# of units rehabbed

__________Other types of housing programs. Please specify__________

____

Did you use any type of private investment to leverage funds? ( )yes; ( )no

Specify the arrangement:

Estimate the ratio of public to private funds:__________

Have your housing programs been used to:

__________bring property up to local codes & standards

__________conserve energy

__________general property improvements

Can you estimate how many homes were privately rehabbed because there was local CDBG rehabilitation taking place in a neighborhood?__________

Check the following impacts which rehab has had.

__________increased property value

__________stabilized neighborhoods

__________visual improvement

__________energy conservation

__________increased local taxes

__________increased job opportunities

__________public health & safety improvements

__________other (please specify)__________

What percentage of these housing activities have benefited low and moderate income persons?__________

Public Services

What types of public services has your CDBG program funded in the past?

______health services for elderly or other special groups

______social services for elderly

______buildings for special purposes

_________job training, please estimate the number of placements_______

_________child care

_________other, please specify________

____

How will the reduction in non-CDBG funded social, public services affect your program? (Check one)

_________No impact on CDBG

_________Will put political pressure on funds

_________Will likely be funded out of CDBG at expense of other activities

_________Other impacts (please specify)

Other

Are there any other CDBG funded activities that have been particularly significant in your community, such as commercial rehabilitation or other economic development activities?

3. IMPACT OF FUNDING REDUCTIONS

What has been the effect of past reductions in CDBG funding? What specifically has the community done to cope with a reduction in funding for CDBG?

Work on on-going projects been slowed down: ( )yes; ( )no. Please specify:

Projects planned have been abandoned? ( )yes; ( )no. Please specify:

Emphasis of program shifted, such as from physical development work to service delivery, for instance: ( )yes; ( )no.

Is your program shifting more to service delivery? ( )yes; ( )no

If yes, what is the reason for this? Please be specific:

Are other types of shifts taking place?

What estimates can you make for future funding needs?

For public works? $__________ For public services? $____________

For housing? $__________, ________units Other? $_________________

What do you estimate are the unmet needs of your community?

For public works? $___________ For public services? $____________

For housing? $__________, ______units Other? $_________________

BEST DOCUMENT AVAILABLE

4. OBLIGATED CDBG, UDAG, SEC. 108 FUNDS

Many cities are obligated to provide new or substantially rehabilitated assisted housing units as a result of planned activities; urban renewal plans, court settlements or HUD directives (i.e., conditions and grant agreements; performance reviews and audits) and have committed CDBG, UDAG or Sec. 108 loan guarantee funds toward this effort, on the expectation of receiving assisted housing units from HUD. If the form of assisted housing anticipated from HUD is terminated, will you have obligations which you cannot meet, as a result of:

______a.	replacement housing for relocation act requirements	______# of units
______b.	court settlements	______# of units
______c.	HUD performance reviews	______# of units
______d.	HUD audits	______# of units
______e.	planned activities	______# of units
______f.	urban renewal	______# of units
______g.	pending projects	______# of units
______h.	others (please specify)______________________ ____________________________________	______# of units

What CDBG funds have you committed to these efforts on the expectation of receiving assisted housing funds from HUD? For:

$__________land acquisition
$__________site clearance
$__________buying buildings for rehabilitation
$__________site improvements
$__________plans and specification
$__________in anticipation of low interest bonds becoming available for Sec. 8
$__________other (please specify)

5. VIGNETTE QUESTIONS

A. If you were to take David Stockman, Director of OMB on a tour of your city, what two or three projects would you show him as examples of successful and necessary expenditures of CDBG funds? What positive impacts has CDBG had in your community that might convince Mr. Stockman of the importance of the program?

B. If your local Congressman wanted to know what on-going or planned projects would fall through as a result of cutbacks in CDBG what would you tell him or her? Can you estimate losses in terms of jobs, revenues, developments? Can you come up with other funding sources for any of these losses?

C. Have any noteworthy projects expecting a UDAG been denied or rejected from that program not on the project's merits, but from lack of enough UDAG funds? What has that loss meant to your community?

5. URBAN DEVELOPMENT ACTION GRANTS

Are you a UDAG-eligible community? ( )yes; ( ) no

Have you received UDAG funds in the past? ( )yes; ( )no When was the last time you received a grant?______________, and what has been your total number and amount of grants received (#)________________ for a total of $________________.

Please list the projects and describe them briefly. Also indicate by "L" and/or "G" whether the UDAG was a grant and/or loan.

Project	Purpose	Amount	Jobs Created/ Retained	$ Leverage Ratio	Equity	Revolving Loan Funds
Total:		______	______	______	______	______

Have any of your UDAGs been for housing productions? ( )yes; ( )no. If so, please describe each project, and list how many units of housing and what kind were produced:

Project	Purpose	# of Units	Rental/Homeowner

Thank you for your time. The answers you have provided for this survey will be compiled, and a copy sent to you for your information and use. We believe that this information will be very helpful to our efforts in Washington to build support for the fully authorized level of funding for CDBG and UDAG. Your help in this effort is extremely valuable.

Chairman GONZALEZ. Thank you very much, Mr. Jones. Let me just say this. I do not know, either, what it is going to take unless it is the whole thing falling around our ears.

I notice you said what is it going to take. I really do not know. I am sweating it out. For instance, we are talking about even assuring you a flow of flat allocation as long as you have some stability. Well, we are about to enter into the throes of another battle which will soon be in the papers. It is not right now because we have to get the continuing resolution before the end of this month.

So even the Congress itself has not resolved that. Ever since the last Congress we have been operating on a continuing resolution on appropriations.

I wanted to thank you, though, and thank NAHRO which always has come through. And we will proceed with the next panelist and then we will go into the question and answer period. Mr. McCauley?

STATEMENT OF JOHN A. McCAULEY, DEPUTY COMMISSIONER, DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT, CITY OF BALTIMORE, SPOKESMAN, COUNCIL OF LARGE PUBLIC HOUSING AUTHORITIES

Mr. McCAULEY. Good afternoon, Mr. Chairman and members of the committee. My name is John McCauley, and I am deputy director of the Baltimore Department of Housing and Community Development.

I am here today as a spokesman for the Council of Large Public Housing Authorities. The council was formed last year as a response to the unprecedented crisis that faced public housing authorities as a result of HUD's refusal to ask the Congress for adequate funding for public housing operating subsidies. I am here today to tell you that the situation this year is much worse than it was last year, and the outlook for the future is exceedingly grim.

It is no longer an exaggeration to say that if the administration succeeds in its current proposals, within a few years there will no longer be any public housing in this country that can provide shelter for low-income people.

The Department of Housing and Urban Development appears to be engaged in a war on public housing with the objective of terminating the Federal commitment to this program as soon as it can do so. Behind a smokescreen of rhetoric about the new federalism, HUD proposes to turn public housing over to the local level or to the private sector, well aware of the fact that without Federal subsidies, neither can afford to continue this program unless they simply evict low-income tenants from the units.

I come before your committee, Representative Gonazalez, well aware that you and the committee members have always shown a strong commitment to keeping public housing as a program for the poor, to providing the needed operating subsidies for this housing and to authorizing much needed modernization funds to maintain the quality of public housing. The council thanks you for this commitment. Your thorough understanding and familiarity with this program has made you a guardian for the poor and the unfortunate of this country.

I would like to begin my remarks with some comments regarding your committee's proposed, "Housing Act of 1982—A Positive Program."

One, operating subsidies. As you are well aware, there are over 1.2 million public housing units in the Nation providing shelter for over 3.5 million lower income Americans. The value of these units is presently estimated at over $70 billion. Without adequate funds for operations, maintenance and security, deterioration of these units will result in many units being lost permanently due to dilapidation, crime and vandalism.

The Federal operating subsidy provides the funds that public housing authorities need to carry out these important functions and still be able to charge affordable rents to low-income households. We support the committee's authorization, $1.6 billion for public housing operating subsidies in fiscal year 1983.

This represents approximately 11.4 percent increase over the council's estimate of what is needed in fiscal year 82, $1.4 billion. In normal times, this would appear to be adequate to fully fund the public housing performance funding system at 100 percent of the level the council estimates is needed for fiscal year 1983.

However, Mr. Chairman, these are not normal times. A variety of proposals are being made by the administration that are going to reduce the income of poor people in general and of public housing tenants in particular, which could result in a need for operating subsidies greater than those currently projected. Although we do not know the full consequences of these proposals at the present time, we know that your committee will be sensitive to this situation as further information becomes available.

Two, the council supports your renewal of a $2 billion authorization for modernizing public housing and your requirement that the Secretary of the Department of Housing and Urban Development shall enter into contracts aggregating at least $85 million during the fiscal year. The modernization program is essential for continuing the livability of the public housing stock.

We hope that the appropriation level will exceed the minimum that you had mandated. The administration has requested $90 million. I also have some comments to make regarding the council's proposals for using modernization funds as part of the public housing energy conservation program. And I will return to this subject later in my remarks.

Three, the public housing development. The council also commends the committee for authorizing additional public housing development money that would result in approximately 20,000 units of public housing. The Reagan administration has recently proposed rescissions in $9.4 billion, most of it for the development of low-income housing.

At the same time, the President is reportedly now considering $1 billion in aid for mortgage assistance for middle-income families, in order to stimulate the construction industry.

Mr. Chairman, authorizing additional modernization and development for public housing will both provide a boost for the construction industry and at the same time, direct the Federal Government's resources towards those who are most in need, for use of development funds for operating subsidy.

Four, use of development funds for operating subsidy. Mr. Chairman, we understand why this committee has included in this year's bill a provision for authorizing public housing authority for using part or all of its development funds for operating subsidy in the current year.

There are some large, severely distressed PHA's who desperately need additional funding if they are to survive. It makes little sense for these PHA's to develop new units when they cannot operate the units they already have. We are concerned, however, that in the current administration, HUD, will seize upon this provision as a way of opening the door of a variety of manipulations that could eventually result in PHA's getting less, not more funds for their operations.

HUD may find ways to force all PHA's to give up all development funds for this purpose, either directly or indirectly, even in areas where new units are greatly needed.

In addition, HUD could use this provision to avoid asking Congress for the level of operating subsidies that are actually needed.

The council would therefore, like to request the committee, if it does authorize such transfers, to limit and personally the total amount that can be transferred in this manner. The council prefers allowing PHA's the choice of using development funds for the modernization program and would furthermore, like to limit HUD's ability to require PHA's to return a portion of previously allocated development money to HUD as a condition for this transfer.

Five, rulemaking to cover the shortfall. My final comment with respect to the proposed Housing Act of 1982, relates to the provision that when there is a deficiency in the amount available to HUD for operating subsidy, the method of allocating the shortfall shall be considered to be a rulemaking activity of the Secretary, which rulemaking activity must come under the Administrative Procedures Act.

We have met with the committee's staff in the past on this issue and we share with them our common frustration of HUD's inordinate delays and arbitrary methods for developing procedures for allocating the shortfall in current fiscal year 1982 funds.

HUD has not put any of this money into the hands of PHA's to date, and it is also trying to force PHA's to sign off on their final payment for fiscal year 1981, by giving up their claims to utility adjustments that would normally be paid out of fiscal year 1982 money.

The reason HUD is going for this illegal requirement, is that when there is a shortfall, HUD claims to have unlimited discretion to change all of the operating subsidy allocations procedures, regardless of the regulations.

Clearly, HUD cannot be allowed to continue to flout its own regulations in this manner. The council would like to work with your staff to further refine the language of this provision. For example, we would like to recommend that HUD be required to publish in the Federal Register each fall, the calculations of operating subsidy needs which are produced by the PFS model unadjusted by political considerations.

We also, recommend that HUD be required to submit to Congress, within a reasonable time, after the President's budget message, an update of these calculations based upon the most recently available information.

The language of the statute should contain an acknowledgement of the fact that the original estimation of operating subsidy needs under the PFS system, occurs long before the actual expenditures occur and that these early estimates are expected by Congress to be revised, when more recent information becomes available. And that Congress expects that there will be an interactive process between HUD and the Congress in order to make these adjustments on a timely basis.

Mr. Chairman, I would now like to proceed to several other matters that the council would like to bring to your attention.

The first is a deep distrust being felt by PHA's as a result of HUD's current policies and actions. During 1981, the Department's attack took the form primarily of not requesting adequate funds for the performance funding system. This year, however, HUD's campaign is more active and aggressive and will ultimately be more devastating.

In 1982, the administration is using every method at its disposal to frustrate the effective administration of the public housing program. And it is becoming clear, that HUD is taking these actions in order to make the administration of housing by PHA's impossible, so that HUD's policies will become self-fulfilling prophecies and there will be no alternative but for PHA's to close down and turn the units over to the private sector.

If HUD's current efforts are allowed to continue, in their present form, I seriously believe that many public housing authorities will be unable to operate by the end of 1983 and there will be little left to revive, even if HUD's policies change at some future date.

Some of the topics that HUD is using against PHA's and tenants include the following:

First, long delays in issuing already appropriated operating subsidies. Although Congress has provided $1.152 billion in operating subsidies for fiscal year 1982, no PHA's have yet received any of this money in hand. The PHA's which began their fiscal years in January 1, a group which includes most of the largest PHA's and which ultimately receives an average of 40 percent of the operating subsidy each year, are now into their third month of operations for the year without an approved budget from HUD.

Much worse, when these budgets are approved by HUD, they will be approved at a level of only 75 percent of the acknowledged need during the fiscal year 1981, not including utility adjustments. This represents approximately 60 percent of what these PHA's need in fiscal year 1982.

HUD claims that this level of allocation is necessary, while it delays the allocation of the rest of the money.

Mr. Chairman, this is a disastrous situation for these authorities.

Second, the manipulation of operating subsidy needs. OMB began this fiscal year by deducting 5 percent of the funds appropriated by Congress whereas no cut was required. Since then, HUD's manipulations have become increasingly ridiculous as the Department attempts to prove that there is no shortfall in the operating subsidies in the fiscal year 1982.

Calculations developed by the Council of Large Public Housing Authorities, indicate that there is indeed a shortfall this year in the amount of approximately $250 million, representing the difference between the $1.152 billion currently available and the council's estimate of the need, which is $1.401 billion dollars.

Last fall, HUD's estimate of the need was $1.37 billion. The council's estimate differs from this estimate only in that we estimate that $13 million less in revenues will be received by PHA's due to the increase in rent income ratios this year.

The regulations have not yet been issued by HUD. And that $17 million more will be needed for an insurance fund.

Since last fall, however, HUD has come up with an additional $218 million in cuts, in the operating subsidy by torturing the PFS calculations so that HUD's official estimate of operating subsidy needs, for fiscal year 1982, is now $1.152 billion, exactly the amount already approved by the Appropriations Committee.

HUD therefore, claims there is no shortfall. Mr. Chairman, we ask you to join with us in trying to prevent HUD from making a mockery of the performance funding system in this way. HUD is taking some elaborate and fairly sophisticated calculations generated by a computer model, which was developed on the basis of extensive research and revisions over the years, and then chopping down the outputs to fit the procrustean bed of its own politically determined budget estimates.

It is obviously an exercise in futility for HUD to carry out an internal evaluation of the performance funding system if HUD is going to totally distort the output of the PFS in this way.

The excuses that HUD has come up with to eliminate the shortfall this year include the following:

First, reducing utility consumption by 10 percent at a value of $103.6 million; mandatory payback in energy costs due to modernization, at a value of $40 million; unspecified State and local contributions, at a value of $41.6 million; unspecified cost reductions due to deregulation, at $20 million; and an arbitrary reduction in the nonutility inflation rate, at a value of $12.8, totalling, $218.

Mr. Chairman, the council believes that these reductions are a figment of HUD's imagination, and have no basis in reality. We are not aware of any information that HUD has that can justify these calculations.

We are convinced that the procedures that HUD is proposing to mandate the reduction in utility consumption figures are irresponsible. We know of no way that $40 million in additional State and local funds, for example are going to made available to public housing.

Third, delaying actions and actions contrary to regulations. In addition to delays in allocating the money and requesting too little, HUD is taking further actions that obstruct the effective administration of the Public Housing Program:

A. The Department has announced its intentions not to pay utility adjustments out of fiscal year 1982 appropriations. This would hold back as much as $65 million in funds that PHA's would otherwise legitimately be entitled to.

B. HUD is requiring, under duress, all PHA's to agree to relinquish these funds as a condition to receiving their final allocation for fiscal year 1981 funds. We have advised PHA's to sign off on this condition without giving up their rights to take future legal action against the Department.

C. The Department is issuing new requirements that HUD regional offices calculate private market energy consumption rates in an effort to cut public housing energy consumption allowances, although, in most cases, private market housing is not comparable to public housing in its physical condition and other characteristics. The failure of HUD to adequately provide modernization funds is not considered in these calculations.

D. The Department has still been unable to devise a method for allocating the fiscal year 1982 shortfall.

E. The Department has announced its intention to review the fiscal year 1982 budgets of the 50 largest PHA's in the central office, thereby, further seriously contributing to additional delays. The Department has hinted that it is developing additional cost standards for such PHA's, although these would be contrary to the standards already in place under the performance funding system.

The HUD central office repeatedly complains of local PHA waste and mismanagement. It is time for HUD to start getting its own house in order. Local PHA's cannot manage public housing when HUD withholds available, and will not tell them how much they can expect to receive during the year, or when HUD carries out a program of systematic harrassment of PHA's, through a variety of administrative obstacles and delays.

Fourth, HUD's intents to "privatize" public housing. At the same time that HUD is contributing to the destruction of PHA's it is pressing ahead with its misguided policies of privatizing public housing and turning it over to local government, or to the private sector.

HUD is now conducting field studies intended to lay the basis for marketing public housing to the private sector. In addition, local management oversight and review committees, so called, MORC's, are being established with the aim of transferring responsibility for public housing back to the local level.

The following is a quote from a HUD memo concerning the MORC program, and I quote: "Under mayoral leadership, the MORC's, with local private sector participation, will be working to a local independence in the provision of public housing."

Mr. Chairman, the Council of Large Public Housing Authorities, believes that the continuing Federal operating subsidies, and other assistance, will always be required in the future, in order to enable public housing to house low-income people. There is no other way. Neither localities nor the private sector have or are willing to allocate the kinds of resources that are needed to sustain these activities.

We ask that your committee continue to support the Federal presence in the public housing field and to keep HUD from carrying out its present misguided policies.

I would like now to turn to some specific positive proposals of our own, which the Council of Large Public Housing Authorities would like to make for improving the administration of the public housing program.

First, a recommended program for energy conservation in public housing. Mr. Chairman, in contrast to the administrative manipulations which HUD is now trying to carry out, contrary to its own regulations, we have a positive program for energy conservation, in public housing. It is comprehensive, it can work.

Our program includes the following components:

First, maintaining the energy conservation incentives now built into the performance funding system;

Second, providing adequate modernization funds for energy conservation;

Third, adopting a fair procedure for calculating the utility consumption base;

Fourth, allowing PHA's to establish energy conservation reserve funds to draw upon to make conservation related capital improvements and leverage private funding for such improvements;

Fifth, greater HUD involvement in assessing its own data, identifying PHA's with high average consumption, targeting these PHA's for energy audits and a followup to determine what physical and management steps need to be done to correct these situations, and what resources are needed;

Finally, a more significant program of HUD research into ways that the PHA's can reduce energy costs, including publication and distribution of this information, and followup with technical assistance.

Second, recommendations for improving the performance funding system.

The council has also developed a set of recommendations for improving the performance funding system. The following draft recommendations were developed at the council's meeting in Boston in January. They are currently being reviewed by council members. I anticipate few substantial changes.

First, improved management incentives;

Second, PFS adjustments including annual inflation adjustments;

Third, energy related improvements to PFS;

Fourth, an appeals process;

Fifth, consideration of distinctions among categories of PHA's;

Sixth, simplification of PFS work sheets; and

Seventh, relationship of modernization and development funds to the operating subsidy.

The council's priorities within these suggested changes are one and two.

In conclusion, let me say, Mr. Chairman, and members of the committee, thank you, for your attention. In closing, I would like to quote from the findings of a recent report prepared by the surveys and investigations team of your colleagues on the House Appropriations Committee. The report concludes with the following paragraph:

> Public housing is a program for the needy. Unfortunately, many PHA's are confronted with tenants subject to severe poverty, unemployment, vandalism, and crime. These factors make the administration of the program difficult and the operation very costly. The investigative staff believes that the objective and character of the program must constantly be kept in focus. Public housing accounts for 1.5 percent of the 81 million units in America, but furnishes what the private sector cannot—decent housing for over 3 million needy people.

We want to work with you and your committee to insure that public housing can continue to play this role in the future.

Mr. Chairman, thank you, very much.

[Mr. McCauley's prepared statement, on behalf of the Council of Large Public Housing Authorities, follows:]

PREPARED STATEMENT OF JOHN A. MCCAULEY, BALTIMORE DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT

A. INTRODUCTION

Good afternoon Mr. Chairman and members of the Committee. My name is John A. McCauley and I am Deputy Director of the Baltimore Department of Housing and Community Development. I am here today as a spokesman for the Council of Large Public Housing Authorities. The Council was formed last year as a response to the unprecedented crisis that faced Public Housing Authorities as a result of HUD's refusal to ask the Congress for adequate funding for public housing operating subsidies. I am here today to tell you that the situation this year is much worse than it was last year, and the outlook for the future is exceedingly grim. It is no longer an exaggeration to say that if the Administration succeeds in its current proposals, within a few years there will no longer be any public housing in this country that can provide shelter for low-income people. The Department of Housing and Urban Development appears to be engaged in a war on public housing, with the objective of terminating the federal commitment to this program as soon as it can do so. Behind a smokescreen of rhetoric about "the new federalism," HUD proposes to turn public housing over to the local level or to the private sector, well aware of the fact that without federal subsidies neither can afford to continue this program unless they simply evict low income tenants from the units.

I come before your Committee, Rep. Gonzalez, well aware that you and the Committee members have always shown a strong commitment to keeping public housing as a program for the poor, to providing the needed operating subsidies for this housing, and to authorizing much-needed modernization funds to maintain the quality of public housing. The Council thanks you for this commitment. Your thorough understanding and familiarity with this program has made you a guardian for the poor and the unfortunate of this country.

I would like to begin my remarks with some comments regarding your Committee's proposed "Housing Act of 1982 -- A Positive Program."

B. COMMENTS ON SUB-COMMITTEE'S PROPOSED HOUSING ACT OF 1982.

Mr. Chairman and members of the Committee, the Council of Large Public Housing Authorities is deeply gratified by your Committee's continued commitment to adequate funding for the nation's public housing program.

1. Operating subsidies. As you are well aware, there are over 1.2 million public housing units in the nation providing shelter for over 3.5 million lower-income Americans. The value of these units is currently estimted at over $70 billion. Without adequate funds for operations, maintenance and security, deterioration in these units will result in many units being lost permanently due to dilapidation, crime and vandalism. The federal operating subsidy provides the funds that Public Housing Authorities (PHAs) need to carry out these important functions and still be able to charge affordable rents to low income households.

We support the Committee's authorization of $1.6 billion for public housing operating subsidies in FY83. This represents approximately an 11.4% increase over the Council's estimate of what is needed in FY82, $1.401 billion.

In normal times, this would appear to be adequate to fully fund the public housing Performance Funding System at 100% of the level the Council estimates is needed for FY83.

However, Mr. Chairman, these are not normal times. A variety of proposals are being made by the Administration that are going to reduce the income of poor people in general and of public housing tenants in particular, which could result in a need for operating subsidies greater than those currently projected. Although we do not know the full consequences of these proposals at the present time, we know that your Committee will be sensitive to this situation as further information becomes available.

2. Modernization funds. The Council supports your renewal of a $2 billion authorization for modernizing public housing, and your requirement that the Secretary of the Department of Housing and Urban Development shall enter into contracts aggregating at least $85 million during the Fiscal Year. The modernization program is essential for continuing the livability of the public housing stock.

We hope that the Appropriations level will exceed the minimum you have mandated. The Administration has requested $90 million.

I also have some comments to make regarding the Council's proposals for using modernization funds as part of a public housing energy conservation program, and I will return to this subject later in my remarks.

3. Public housing development. The Council also commends the Committee for authorizing additional public housing development money that would result in approximately 20,000 units of public housing.

The Reagan Administration has recently proposed rescissions in $9.4 billion, most of it for the development of low-income housing. At the same time, the President is reportedly now considering $1 billion in aid for mortgage assistance for middle-income families, in order to stimulate the construction industry. Mr. Chairman, authorizing additional modernization and development funds for public housing will both provide a boost for the construction industry, and at the same time direct the federal government's resources toward those who are most in need.

4. Use of development funds for operating subsidy. Mr. Chairman, we understand why this Committee has included in this year's bill a provision for authorizing a PHA to use part or all of its development funds for operating subsidy in the current year. There are some large, severely distressed PHAs that desperately need additional funding if they are to survive. It makes little sense for these PHAs to develop new units when they cannot operate the units they already have.

We are concerned, however, that in the current Administration HUD will seize upon this provision as a way of opening the door to a variety of manipulations that could eventually result in PHAs getting less, not more, funds for their operations. HUD may find ways to force all PHAs to give up all development funds for this purpose, either directly or indirectly, even in areas where new units are greatly needed. In addition, HUD could use this provision to avoid asking Congress for the level of operating subsidies that are actually needed.

The Council would therefore like to request the Committee, if it does authorize such transfers, to limit and closely monitor the total amount that can be transferred in this manner.

The Council prefers allowing PHAs the choice of using development funds for the modernization program, and would furthermore like to limit HUD's ability to require PHAs to return a portion of previously allocated development money to HUD as a condition of this transfer.

5. Rule-making to cover the short-fall. My final comment with respect to the proposed Housing Act of 1982 relates to the provision that when there is a deficiency in the amount available to HUD for operating subsidy, the method of allocating the short-fall

shall be considered to be a rule-making activity of the Secretary, which rule-making activity must come under the Administrative Procedures Act.

We have met with the Committee's staff in the past on this issue and have shared with them our common frustration at HUD's inordinate delays and arbitrary methods for developing procedures for allocating the short-fall in current FY82 funds. HUD has not put any of this money into the hands of PHAs to date, and is also trying to force PHAs to sign off on their final payment for FY81 by giving up their claims to utility adjustments that would normally be paid out of FY82 money. The reason HUD is giving for this illegal requirement is that when there is a short-fall, HUD claims to have unlimited discretion to change all of the operating subsidy allocation procedures, regardless of the regulations. Clearly, HUD cannot be allowed to continue to flout its own regulations in this manner.

The Council would like to work with your staff to further refine the language of this provision. For example, we would like to recommend that HUD be required to publish in the Federal Register each Fall the calculations of operating subsidy needs which are produced by the PFS model, unadjusted by political considerations. We also recommend that HUD be required to submit to Congress, within a reasonable time after the President's Budget Message, an up-date of these calculations based upon the most recently available information.

The language of the statute should contain an acknowledgement of the facts that the original estimation of operating subsidy needs under the PFS system occurs long before the actual expenditures occur; that these early estimates are expected by Congress to be revised when more recent information becomes available; and that Congress expects there will be an inter-active process between HUD and the Congress in order to make these adjustments on a timely basis.

Mr. Chairman, I would now like to proceed to several other matters that the Council would like to bring to your attention.

The first is the deep distress being felt by PHAs as the result of HUD's current policies and actions.

C. HUD'S WAR ON PUBLIC HOUSING: REVIEW OF CURRENT PROBLEMS BEING FACED BY PUBLIC HOUSING AUTHORITIES.

Mr. Chairman and members of the Committee, I would like to review with you some of the current actions being taken by HUD that are so serious that they can only be called a war on public housing. I and other members of the Council are deeply outraged at this all-out attack on the public housing system.

During 1981, the Department's attack took the form primarily of not requesting adequate funds for the Performance Funding System.

This year, however, HUD's campaign is more active and aggressive and will ultimately be more devastating.

In 1982, the Administration is using every method at its disposal to frustrate the effective administration of the public housing program. It is becoming clear that HUD is taking these actions in order to make the administration of public housing by PHAs impossible, so that HUD's policies will become self-fulfilling prophecies and there will be no alternative but for PHAs to close down and turn the units over to the private sector. If HUD's current efforts are allowed to continue in their present form, I seriously believe that public housing will be destroyed by the end of 1983, and that there will be little left to revive even if HUD's policies change at some future date.

Some of the tactics which HUD is using against Public Housing Authorities and tenants include the following.

1. Long delays in issuing already appropriated operating subsidies. Although Congress has provided $1.152 billion in operating subsidies for FY82, no PHAs have yet received any of this money in hand. The PHAs which begin their Fiscal Years on January 1, a group which includes most of the largest PHAs and which ultimately receives an average of

forty per cent of the operating subsidy each year, are now into their third month of operations for the year without an approved budget from HUD. Much worse, when these budgets are approved by HUD, they will be approved at a level of only 75% of the acknowledged need during FY81, not including utility adjustments. This represents approximately 60% of what these PHAs need in FY82. HUD claims this level of allocation is necessary while it delays the allocation of the rest of the money. Mr. Chairman. this is a disastrous situation for these Authorities.

2. Manipulation of operating subsidy needs. OMB began this Fiscal Year by deducting 5% of the funds appropriated by Congress, whereas only 4% was required. Since then, HUD's manipulations have become increasingly ridiculous as the Department attempts to prove that there is no short-fall in operating subsidies in FY82.

Calculations developed by the Council of Large Public Housing Authorities indicate that there is indeed a short-fall this year, in the amount of approximately $250 million, representing the difference between the $1.152 billion currently available and the Council's estimate of the need, which is $1.401 billion. (See Figure 1.)

Last Fall, HUD's estimate of the need was $1.370 billion. The Council's estimate differs from this estimate only in that we estimate that $30 million less in revenues will be received by PHAs due to the increase in rent-income ratios this year (the regulations have not yet been issued by HUD), and that $17 million more will be needed for an insurance fund.

Since last Fall, however, HUD has come up with an additional $218 million in cuts in the operating subsidy, by torturing the PFS calculations, so that HUD's official estimate of operating subsidy needs for FY82 is now $1.152 billion, exactly the amount already approved by the Appropriations Committees. HUD therefore claims there is no short-fall.

Mr. Chairman, we ask you to join with us in trying to prevent HUD from making a mockery of the Performance Funding System in this way. HUD is taking some elaborate and fairly sophisticated calculations generated by a computer model which was developed on the basis of extensive research and revisions over the years, and then chopping down the outputs to fit the Procrustean Bed of its own politically-determined budget estimates.

It is obviously an exercise in futility for HUD to carry out an internal evaluation of the Performance Funding System if HUD is going to totally distort the output of the PFS in this way.

The excuses HUD has come up with to eliminate the short-fall this year include the following:

a)	Reduce utility consumption by 10%	$103.6 million
b)	Mandatory paybacks in energy costs due modernization	40.0
c)	Unspecified state and local contributions	41.6
d)	Unspecified cost reductions due to "de-regulation"	20.0
e)	Arbitrary reduction in the non-utility inflation rate	12.8
	TOTAL	$218.0 million

Mr. Chairman, the Council believes that these reductions are the figment of HUD's imagination, and have no basis in reality.

We are not aware of any information which HUD has which can justify these calculations. We are convinced that the procedures that HUD is proposing to mandate/ the reduction in utility consumption figures are irresponsible.

We know of no way that $40 million in additional state and local funds are going to be made available to public housing.

3. Delaying actions and actions contrary to regulations. In addition to delays in allocating the money, and requesting too little, HUD is taking further actions that obstruct the effective administration of the public housing program.

a) The Department has announced its intention not to pay utility adjustments out of FY82 appropriations. This would hold back as much as $65 million in funds PHAs would otherwise legitimately be entitled to.

b) HUD is requiring, under duress, all PHAs to agree to relinquish these funds as a condition of receiving their final allocation of FY81 funds. We have advised PHAs to sign-off on this condition without giving up their rights to take future legal action against the Department.

c) The Department is issuing new requirements that HUD Regional Offices calculate private market energy consumption rates in an effort to cut public housing energy consumption allowances -- although in most cases private market housing is not comparable to public housing in its physical condition and other characteristics. The failure of HUD to adequately provide modernization funds is not considered in these calculations.

d) The Department has still be unable to devise a method for allocating the FY82 short-fall.

e) The Department has announced its intention to review the FY82 budgets of the 50 largest PHAs in the Central Office, thereby further seriously contributing to additional delays. The Department has hinted that it is developing additional cost standards for such PHAs, although these would be contrary to the standards already in place under the Performance Funding System.

The HUD Central Office repeatedly complains of local PHA waste and mismanagement. It is time for HUD to start getting its own house in order. Local PHAs cannot manage public housing when HUD withholds available funds and will not tell them how much they can expect to receive during the year, or when HUD carries out a program of systematic harrassment of PHAs through a variety of administrative obstacles and delays.

4. HUD's intent to "privatize" public housing. At the same time that HUD is contributing to the destruction of PHAs, it is pressing ahead with its misguided policies of "privatizing" public housing and turning it over to local government or to the private sector. HUD is now conducting field studies intended to lay the basis for marketing public housing to the private sector.

In addition, local Management Oversight and Review Committees (MORCs) are being established with the aim of transferring responsibility for public housing back to the local level. The following is a quote from a HUD memo concerning the MORC program:

> "....Under Mayoral leadership the MORCs, with local private sector participation, will be working to a local independence in the provision of public housing." (emphasis added)

Mr. Chairman, the Council of Large Public Housing Authorities believes that continuing federal operating subsidies and other assistance will always be required in the future in order to enable public housing to house low income people. There is no other way. Neither localities nor the private sector have, or are willing to allocate, the kinds of resources that are needed to sustain these activities.

We ask that your Committee continue to support the federal presence in the public housing field, and to keep HUD from carrying out its present misguided policies.

I would now like to turn to some specific positive proposals of our own which the Council of Large Public Housing Authorities would like to make for improving the administration of the public housing program.

FIGURE 1

ESTIMATED NEED FOR FY82 PUBLIC HOUSING OPERATING SUBSIDY.

($ millions)

	HUD Est.	CLPHA* Est.
Allowable Expense Level (AEL)	1469	1469
Utilities	1104	1104
IPA (audit)	4	5
Income, with no change in rent-income ratios	(1221)	(1221)
PFS BASE	1356	1357
Increased rent-income-ratios		
- All tenants to 26%	(25)	(15)
- New tenants to 30%	(8)	(5)
Insurance costs	0	17
Non-PFS Authorities	47	47
TOTAL	1370	1401

Miscellaneous recent adjustments by HUD

- Reduction in utility consumption base by 10%	(103.6)
- Payback from energy modernization funding	(40.0)
- State and local government contributions	(41.6)
- Cost reductions due to de-regulation	(20.0)
- Reductions in non-utility inflation rate to 7.5%	(12.8)
SUB-TOTAL NEW ADJUSTMENTS	(218.0)
TOTAL NEED ACCORDING TO HUD	$1152

*Council of Large Public Housing Authorities

D. A Recommended Program for Energy Conservation in Public Housing.

Mr Chairman, in contrast to the administrative manipulations which HUD is now trying to carry out contrary to its own regulations, we have a positive program for energy conservation in public housing. It is comprehensive. It can work.

Our program includes the following components:

a) maintaining the energy conservation incentives now built into the Performance Funding System;

b) providing adequate modernization funds for energy conservation;

c) adopting a fair procedure for calculating the utility consumption base;

d) allowing PHAs to establish energy conservation reserve funds to draw upon to make conservation-related capital improvements and leverage private funding for such improvements;

e) greater HUD involvement in assessing its own data, identifying PHAs with high average consumption, targeting these PHAs for energy audits, and following up to determine what physical and management steps need to be done to correct these situations, and what resources are needed;

f) a more significant program of HUD research into ways that PHAs can reduce energy costs, including publication and distribution of this information and follow-up with technical assistance.

Attachment II includes a brief additional statement about each of these items.

E. Recommendations for Improving the Performance Funding System.

The Council has also developed a set of recommendations for improving the Performance Funding System. The following Draft recommendations were developed at the Council's meeting in Boston in January. They are currently being reviewed by Council members. I anticipate few substantial changes.

1) Improved management incentives.

2) PFS adjustments including annual inflation adjustments.

3) Energy-related improvements to PFS.

4) An appeals process.

5) Consideration of distinctions among categories of PHAs.

6) Simplification of PFS worksheets.

7) Relationship of modernization and development funds to the operating subsidy.

The Council's priorities are #1 and #2 above.

Attachment I includes a more extensive description of each of these items.

F. CONCLUSION

Mr. Chairman and members of the Committee, thank you for your attention. In closing, I would like to quote from the findings of a recent report prepared by the Surveys and Investigations Team of your colleagues on the House Appropriations Committee. The report concludes with the following paragraph.

> "Public housing is a program for the needy. Unfortunately, many PHAs are confronted with tenants subject to severe poverty, unemployment, vandalism, and crime. These factors make the administration of the program difficult and the operation very costly. The Investigative Staff believes that the objective and character of the program must constantly be kept in focus. Public housing accounts for 1.5 percent of the 81 million units in America but furnishes what the private sector cannot -- decent housing for over 3 million needy people."

We want to work with you and with your Committee to insure
continue to
that public housing can/play this role in the future.

Thank you Mr. Chairman.

ATTACHMENT I: DETAILED RECOMMENDATIONS FOR IMPROVING THE PERFORMANCE FUNDING SYSTEM.

Introduction

The Council of Large Public Housing Authorities (CLPHA) supports a *fully-funded* Performance Funding System (PFS) *in a revised and improved form* as the principal funding mechanism for the nation's conventional public housing program.

Until a better system can be designed, and its impact evaluated, PFS represents the best currently available system that attempts to reflect the true cost of operating public housing, while retaining the principal purpose of public housing: to provide housing for the poor.

CLPHA believes that with the following revisions and improvements, a fully-funded PFS can adequately support the operations of PHAs and the tenants they serve.

CLPHA is also aware that a variety of revisions and alternatives to PFS are now under study by HUD, and CLPHA will review these recommendations when they become available to determine what position to take in the future.

CLPHA's priorities are recommendations #1 and #2 below.

1. Management Improvements and Management Incentives

a) Allow PHAs to keep some portion of increases in budgeted income. At the present time, if a PHA can budget an increase in its income for any reason, from one year to the next, its subsidy will be reduced by the same amount. Therefore, there is currently no incentive for the PHA to try to increase its income.

CLPHA believes that there should be some system whereby PHAs are allowed to keep some of this increase in income. Mr. Ray Struyk has made what appears to be one type of effective proposal for accomplishing this end. The Struyk proposal would allow a PHA to deduct only 85% of any increase in income from the amount of subsidy received. This would have a cumulative effect over the years, as the budgeted income for PFS calculations would increasingly grow smaller than actual PHA income. Struyk proposes a limit on the savings at the point where budgeted income has been reduced to 80% of actual PHA income. It would take a number of years, however, before a PHA would actually reach that point.

In order to insure that these funds were used for the PHAs highest priorities, it would be possible to consider mandating that the funds be put into a capital improvements or energy conservation reserve fund, provided that doing so did not result in the PHA's losing its modernization funding to a comparable degree.

b) Vacant units. Allow PHAs to keep all rental income that is collected above an established occupancy rate, e.g. 95%, in current and subsequent years, in order to provide an incentive for lowering the vacancy rate.

c) Ceiling rents. Continue to permit PHAs to establish ceiling rents. In many PHAs, ceiling rents are needed to maintain an exonomic mix of tenants within public housing. Depending on the local private market, the elimination of ceiling rents could drive out more moderate income tenants from public housing. This would cause more dependence of the PHA on the Federal operating subsidy. More attention needs to be paid by PHAs, however, to adjustments in ceiling rents so that they do not lag far behind comparable private market rent increases.

d) Reserves. Reserves are now widely misunderstood as being merely a "cushion" for PHAs, producing interest income to PHAs while adding to the drain on the federal subsidy. In the interests of good management, however, some type of capital improvements reserve for major repairs and replacements is absolutely essential for any well-run real estate operation. PHAs should be allowed to budget an adequate level of annual payments into such reserve funds.

Consideration might also be given to establishing a reserve fund specifically for energy conservation capital improvements. PHAs could be allowed to keep 100% of their increases in income provided that the funds were deposited in this energy conservation reserve account. This same principal could be extended to allow PHAs to keep 100% of the savings realized by reductions in consumption below the utility "base", provided that these savings all went into the energy conservation reserve. For

PHAs in the enviable position of having reach the "maximum reserves" position, they could be allowed to exceed the maximum reserve provided that these funds were targeted to energy improvements and expended within a reasonable time period.

The reserve fund could also be used to leverage additional private investments in public housing energy improvements.

e) Interest income. Eliminate the HUD requirement that PHAs return a portion of their interest earnings to HUD if these earnings exceed HUD's current limits.

2. Adjustments to PFS Formula (including inflation adjustment).

The Allowable Expense Level (AEL) should be adjusted at the end of each Fiscal Year for inflation as is done now with the utilities expense level, to reflect the change between the originally projected inflation rate and the actual inflation rate.

Rather than using the wage-scale index to determine the AEL inflation rate (since wages have been depressed over the past few years compared to other prices), a truer indication of inflation for PHAs would be a composite inflation factor weighted for building materials, insurance costs, employee benefits and the other elements that make up the AEL. This would tend to reduce the type of underestimation of AEL inflation rates that has occurred in past years.

CLPHA agrees with the concept of a retrospective inflation adjustment to make up for underestimation of inflation for previous years.

CLPHA is willing to explore the concept of a two or three year authorization by HUD of a local PHA's AEL, in order to promote better planning and management within the PHA. The second and third year AEL would be calculated by applying the inflation factor to the previous year's AEL as an adjustment. The authorization established by HUD for each PHA would be "subject to available funding" by Congress, and HUD would still have to seek funding for the public housing operating subsidy on an annual basis. CLPHA is opposed to any "cap" on authorizations for the public housing operating subsidy at the FY82 level.

CLPHA also feels that a one-time adjustment should be made to the AEL for those PHAs which were most adversely affected by inadequate base-year funding, either by direct action by HUD or through an appeals process if one were established.

3. Energy-conservation related improvements.

CLPHA strongly supports maintaining year-end utility adjustments, where the prices of utilities have gone up at a more rapid rate than was projected in the utility budget. HUD is now trying to eliminate such adjustments in the FY82 budget, contrary to regulations.

The year-end utility adjustments should be calculated taking degree-days into account.

CLPHA supports maintaining at least the current 50/50 formula whereby a PHA is allowed to retain half the savings it realizes in energy consumption. In addition, CLPHA recommends that PHAs be allowed to retain an even higher proportion if these savings are deposited in an energy conservation reserve account, to be used for energy conservation related capital improvements. This incentive should be strengthened, not weakened by HUD.

Additional energy issues are related to modernization (see Section 7).

4. Appeals Process.

CLPHA supports the concept of an appeals process whereby PHAs can attempt to obtain compensation for what they feel is inadequate funding, either due to inadequate base-year funding or because of costs incurred by the PHA that are not reflected in the current PFS formula, e.g. crime, vandalism, etc. These costs are often associated with the larger urban housing authorities.

There should be strict guidelines for such an appeals process so that only essential appeals would be heard and so that the process would not become totally politicized. Some of the elements of an appeals process could include the following:

- limit of one appeals per PHA every three years;
- rigid time guidelines on determining appeals;
- limit on the amount that could be awarded through the appeals process, per PHA; and,
- have a PHA representative and a professional arbitrator on the Appeals Board.

5. Distinctions among Authorities.

A number of distinctions among PHAs are already factored into the PFS formula. CLPHA is interested in exploring with Congress, HUD and other groups the possibilities of introducing further distinctions into the funding system that would reflect the different approaches appropriate to large, medium, small and troubled PHAs.

One possibility might be to introduce further "range tests" into the formula, for each category of PHA.

Troubled authorities should be dealt with through an appeals process and through MOD and CIAP funding, with funding contingent upon the PHA's improved management capability.

6. Simplifying PFS worksheets.

The "Delta" factor used in calculating the annual subsidy level (per unit month) is intended to reflect the changing circumstances of the PHA. Most of the statistical variables used in calculating "Delta" are actually surrogates for real conditions at the PHA.

(For example, "size of SMSA" is a surrogate for problems associated with large urban PHAs.)

The "Delta" factor is complex to calculate and in practice has little net effect on the change in subsidy level from one year to the next. It is proposed that the "Delta" factor be eliminated at the present time and perhaps be brought back later in a way that is more closely related to actual, significant changes in the PHA's status.

7. Modernization and development funds.

CLPHA recommends that modernization funds not be rolled in with operating subsidy funds, but be retained as a separate entity.

Full and adequate funding of the modernization program is imperative.

CLPHA agrees that the CIAP permits emphasis on energy conservation, but feels that the modernization money currently available is insufficient to support as significant a level of energy conservation improvements as is needed and justified by their potential paybacks. Timely use of modernization funds can save operating expenses in the future, and thereby reduce future dependency on the federal subsidy.

The bulk of the modernization program money should be channeled through CIAP, but HUD should allow a small proportion (reserved for small jobs) to be treated in a flexible fashion by the PHA.

The development program should also be retained, and there should be increased flexibility for PHAs to use previously committed but unused development funds for modernization without returning 50% or more of these funds to HUD as a condition of the transfer.

Attachment II: An Energy Conservation Program for Public Housing.

1) Maintain energy conservation incentives now built into the Performance Funding System.

a) Maintain the 50% share of savings from conservation that PHAs are now allowed to keep; and (also see below) add a new provision that PHAs may be allowed to keep 100% of the savings if they earmark these funds and put them into an energy conservation reserve funds, as long as there are clearly identifiable additional energy conservation measures for which these funds will be expended within a reasonable time.

b) Maintain the system of end-of-the-year utility adjustments now contained in HUDs's own regulations.

2) Adequate modernization funds, tied in with energy conservation planning.

We have supported this Committee's recommendations to adequately fund the modernization program. It is not yet clear how HUD will monitor the modernization program to identify what expenditures are being made for energy conservation purposes, but HUD should explore possible avenues for providing incentives for using the money in this way.

3) Adoption of a fair utility consumption base for PHAs.

Instead of picking private market numbers out of the air, and trying to use them as a basis for establishing allowable consumption levels in public housing -- which is unfair because the public housing stock has entirely different characteristics -- HUD should do its own studies of current PHA utility consumption rates, analyze the reasons for variations among buildings and PHAs, come up with a reasonable consumption ceiling. It should be recognized that many PHAs are unable to bring consumption down to this ceiling without additional modernization spending.

A less normative alternative that could be explored would be to determine the allowable utility consumption base by calculating the average consumption level over the five preceding years for each PHA. If a PHA were conserving energy, its consumption base would gradually decline, but it would still be allowed to keep some of the savings it was producing.

4) Energy conervation reserve fund.

Permit PHAs to keep an additional share of any increases in income they achieve through a variety of means, including reduced energy consumption, provided that these funds are put into an energy conservation reserve fund and earmarked for further future energy conservation improvements, including "leveraging" private irvestments in such improvements.

5) HUD management, monitoring and audits

HUD should exercise closer managerial scrutiny of PHA energy consumption, collect and analyze consumption data, identify those PHAs with apparently high consumption and develop a program for addressing problem projects or PHAs, through a combination of modernization funds, management improvements, energy audits, and other "work-outs."

6) More research

Expanded program of HUD reearch into ways that PHAs can reduce energy costs, and publicizing, distributing and following up on these cases, along with technical assistance to PHAs.

Chairman GONZALEZ. Thank you, Mr. McCauley. The Chair will announce that we must recess in order to allow me to present the section 235 homeownership extension. This act is due to expire at the end of this month and we have a bill extending it placed on the suspension calendar.

[Recess.]

Chairman GONZALEZ. The subcommittee will resume.

I believe at the time we left off Mr. McCauley had concluded his testimony. I believe you had completed your testimony, had you not?

Mr. MCCAULEY. Yes, Mr. Gonzalez, I had completed my testimony. Thank you.

Chairman GONZALEZ. All right, sir.

Excuse me for interrupting again. I have been informed that Mr. Jones has a time constraint. You have a plane to catch?

Mr. JONES. Yes, sir, I do.

Chairman GONZALEZ. Well, we have had all these things come up that we had not anticipated at the time the arrangements were made for this hearing. If there is no objection, I have a couple of questions that I wanted to direct to Mr. Jones, and that way we can free him. Others may wish to submit for the record some questions for the record.

Essentially, are you the chairman of the Michigan State Housing?

Mr. JONES. No, Pontiac, Mich.

Chairman GONZALEZ. The Housing Authority?

Mr. JONES. Yes, sir.

Chairman GONZALEZ. As I understand it, in that area, you have a rather high unemployment rate?

Mr. JONES. We have probably the highest in the State of Michigan, sir, somewhere around 30 percent.

Chairman GONZALEZ. Well, Mr. McCauley gave us some statistics, some projections in reduced income that will result because of the increase in the rental requirements for public housing tenants that the administration has insisted upon.

In your particular area, with this dire economic situation, what do you foresee for the immediate future? In other words, we know that not too long ago, a few weeks ago, we had testimony also to indicate that there were at least three public housing authorities that were confronted with that ugly word, bankruptcy. Is the Pontiac Authority in any real dire immediate situation?

Mr. **Jones**. Yes, sir, we are. If the administration continues to fund the performance funding level at the rates that we have heard they are coming out, we will be bankrupt and out of business within 1 year, sir.

Chairman **Gonzalez**. Within 1 year?

Mr. **Jones**. Within 1 year.

Chairman **Gonzalez**. Do you see anything dire happening even, say, before that date?

Mr. **Jones**. At the 96.5-percent level that they funded us for fiscal year 1981, we will keep our doors open and will be able to provide minimal services to our tenants. The performance funding system at best, sir, is the most inadequate instrument we have ever had and had to use and are faced with, at its best, and now we have been asked to deal with it at 85.5 and 96.5 percent, and then rumors of what the administration promises to do in fiscal years 1982 and 1983 frighten me to the degree that I can assure you we will be out of business, sir.

Chairman **Gonzalez**. Have you had an opportunity to evaluate the possible impact of a rescission such as is presently confronting us? As Mr. McCauley brought out the administration is asking for a $9 billion rescission in assisted housing programs, but we don't know what the House Appropriations Subcommittee has in mind. That means that what you are counting on now and what did you say, 85, 86 percent in 1982?

Mr. **Jones**. For 1981, we did get a supplemental that allowed us to go to 96.5 percent of PFS eligibility.

Chairman **Gonzalez**. OK. Well, suppose a rescission impacts, say, even a reduction in that current commitment. What would be the impact in the Housing Authority of Pontiac? How would you weather it?

Mr. **Jones**. You are talking about the performance funding?

Chairman **Gonzalez**. Yes, sir, because the rescission would be on your ongoing budget.

Mr. **Jones**. What would happen, sir, is probably this. I could overkill the organization. I am going to base my projections for the coming year on the guestimates that are coming out from those leaks you mentioned. In order to be fiscally responsible, I would then have to take certain steps within the organization to make my budget balance. I cannot go into a deficit situation. Now, if that is the case, I must cut the organization, I must reduce its capacity to carry out its prime function to a great degree, or the degree necessary to balance the budget. If I find out that they will give me an adequate supplemental afterwards, it is after I have already overkilled the organization.

What we are really saying to you is that we need some predictability and stability in the situation.

Chairman **Gonzalez**. I see. What about the city? How does it fare with respect to CDBG community development funds, and have they in Michigan or in Pontiac, have they worked in any way by way of allocation in the area of public housing?

Mr. **Jones**. No, sir, they have not in our city.

Chairman GONZALEZ. And does it fare reasonably well in CDBG grants? Does the city of Pontiac get its just share of CDBG grants?

Mr. JONES. As an entitlement city, they get the share that is allocated on the national formula. They do receive it, yes, sir.

Mr. GONZALEZ. I have some more questions for you, which I would request that you answer for the record.

[The following written questions were submitted by Chairman Gonzalez and appear with the responses of Mr. Jones:]

Question 1. It seems to me that the impact of NAHRO's minimum rent proposal would be to move NAHRO away from its 40-year tradition of serving low-income families. Have we come to this just to be able to keep the doors of our housing authorities open?

Answer. NAHRO's proposal is for the locality to have the flexibility to set its own rent schedules; minimum rents is one of the options which would be considered. This flexibility would operate within the framework of the national public housing objective of serving low income people. Our proposal would, additionally, give predictability and stability to the program.

Question 2. Isn't it true that there was a great division among NAHRO's membership about this minimum rent issue, more so than there has been with regard to any other recent major issue?

Answer. Mr. Chairman, there is divided opinion in NAHRO on the issue of minimum rents, however, the consensus of the organization is, as I just indicated, that minimum rents should be an alternative available to PHAs. In response to the concerns raised relating to this issue, NAHRO supports a provision which protects the interests of low income tenants and insures that they have the ability to pay under newly adopted schedules.

Question 3. I ask you to step back in time to the years just before the so-called Brooke amendment which restricted tenant rents to 25 percent of adjusted income. Would you describe the kinds of rent schedules that were in place at that time? Approximately what percentage of their income were the poorest families, those whose income was 30 percent of median or below, paying under those schedules?

Answer. The rent ranged—depending on the size of the household and its income—from 15 percent to about 30 percent. Those whose income was 30 percent of median or below were paying minimum rents which were about 30 percent of their incomes.

Question 4. How can we be assured that permitting PHA's to establish a minimum rent schedule will not result in the poorest families having to look elsewhere for shelter they can afford, to shelter which is indecent, unsafe, and unsanitary?

Answer. In addition to the national objectives and tenant protection language discussed previously, any new rent schedules will be developed in consultation with tenants and approved by HUD. Local housing and elected officials are very sensitive to the realities of public sentiment and tenant rent paying abilities.

Question 5. On page 6 of your testimony, you support, with caution, the use of public housing development funds to cover operating subsidies, citing the benefits of flexibility. But on page 7 you oppose permitting development funds being used for modernization purposes because it forces localities into untenable choices. These positions seem contradictory to me. Are you for local flexibility or are you for providing adequate funding for three separate purposes: operating subsidies, modernization, and production?

Answer. NAHRO supports separate and adequate funding for operating subsidies, CIAP (modernization) and public housing production. In addition to that, we support the local flexibility for PHAs, depending upon local circumstances, to transfer additional money to modernization from its own production pipeline. Our objection to the Administration proposal is that it forces localities to accept the transfer from production to modernization.

Question 6. What is an acceptable rent-to-income ratio for poor families to pay, 35 percent, 40 percent, 50 percent?

Answer. I am unable to categorically state that any specific percentage is an acceptable rent-to-income ratio for poor families to pay. An acceptable rent level is affected by a number of different factors—average rents paid by persons with similar incomes in the private sector, level of welfare assistance, ability to work, age and composition of family. It is for this reason NAHRO suggests localities have the option to establish their own rent schedules which take into consideration rent-to-income ratios as well as other factors.

Chairman GONZALEZ. Well, thank you very much, Mr. Jones.

Mr. JONES. Thank you for the opportunity, Mr. Chairman.

Chairman GONZALEZ. We deeply appreciate your traveling all the way here and giving us your time.

Mr. JONES. It was my pleasure.

Chairman GONZALEZ. We will proceed and recognize Mr. Mooney, executive director of the Chicago Housing Authority.

STATEMENT OF ANDREW J. MOONEY, EXECUTIVE DIRECTOR, CHICAGO HOUSING AUTHORITY

Mr. MOONEY. Thank you, Mr. Chairman. Good afternoon.

My name is Andrew Mooney. I have been executive director of the Chicago Housing Authority for the past 9 months, since June 1981. I am here to describe for you the pain that public housing authorities and their residents are experiencing today as a result of policies currently pursued by the Federal Government.

It is unfortunate that I appear before you at this time, when the Chicago Housing Authority is going through the greatest challenge in its 45-year history. HUD has chosen to single out CHA as its principal public housing antagonist under the guise of mismanagement in order to justify a completely unrealistic public housing budget nationwide.

It is doing so through a HUD-commissioned study recently conducted by Oscar Newman of New York on the Chicago Housing Authority. It is tragic that HUD and the administration are apparently being misled by the report issued as a result of this study. The authority finds the Newman report, as transmitted to us, to be careless and lacking in professional quality. The report's use of outdated statistics and its obvious ignorance of current CHA policies and practices is apparent.

We sincerely believe, as we stated in a letter to Secretary Pierce, that if HUD officials seriously consider the authority's response, the Newman study would be disavowed.

The existence of this report points, however, to the true nature of the debate. It is not a debate simply over the level of funding provided to public housing. It is about the very existence and future of public housing to which this Nation has been so admirably committed.

One may, of course, argue in good faith about the Government's role in public housing. I believe that even though our democracy is based on the fundamental notion of human rights, it must also be fundamentally committed to the common good of the political community. Such a commitment asserts that in order for all citizens to express their rights, everyone must mutually support one another, with the strong assisting the weak, the whole assisting the individual.

It is this commitment, I believe, that underlies the history of public housing in this country, and which is the theoretical basis for the public housing debate we are witnessing today. Before I comment, therefore, Mr. Chairman, on the broad series of issues confronting public housing today, I wish to refer for a few moments to the Newman study on CHA. I should add as I begin that I am taking your time to do this because I feel that this committee must be able to make an independent judgment regarding HUD's credibility and its recommendations regarding the 1982 and 1983 budgets for public housing.

We first learned of the contents of the Newman report in Chicago through the newspapers. Apparently someone, possibly Newman himself, gave the report to the Better Government Association, which in turn offered it to one of the city's major newspapers for publication. The release of this report in this way is unfair in the extreme. It is irresponsible for Federal agents to deal with public housing authorities or any other public agency through the media rather than through direct contact and discussion.

What we find particularly upsetting is that it seems Newman conspired from the beginning to produce a report that would make the authority appear to be a failure regardless of its actual situation. I have already referred to the use of outmoded statistics. I must also add that in several key areas, such as the modernization program and elevator maintenance, Newman deliberately directed the authority to halt its improvements during the study, even though HUD itself had recommended these same improvements.

I need only refer to a few other specific examples where the report errs. Newman comments in his executive summary that at one of our developments we employ several operating engineers and firemen even though we no longer have a central heating plant in operation. It is certainly true that that plant no longer operates. In fact, however, the engineering staff now takes care of over 1,000 multiple boilers and associated equipment separately located in 28 high rise and 4 ancillary buildings.

Newman states in his report that CHA has only 26 requirement purchase orders. In truth, CHA has 59 current requirement purchase orders covering scavenger services alone. Newman also states that CHA has a 2- to 5-year refrigerator replacement period. In fact, CHA has a refrigerator replacement period of approximately 11 years.

Newman states that the authority employs 17 ironworkers and their assistants for its compactor repair unit. Since September 1981, however, we have had only 2 iron workers and 6 compactor laborers on duty. Newman also states that skilled workers are required to unplug toilets and change lightbulbs. In fact, it has always been the case that janitorial staff plunges toilets and replaces lights in public and private spaces in the authority.

Perhaps the worst example of Newman's carelessness has to do with the authority's financial condition, which is of great importance to all of us associated with public housing. I will therefore deal with this issue at length in a moment.

You can see in the examples I have taken from the executive summary of Newman's report that in very critical areas of the authority's operations Newman is simply and completely wrong. The question then arises that if the Newman study is so replete with factual errors, can the recommendations and conclusions have any credibility?

The Chicago Housing Authority does, of course, admit its problems, and has made a determined and conscious effort to initiate major reforms during the past year. The real turning point for the authority came through the deep-felt commitment of Mayor Jane

Byrne to the residents of CHA, as manifest in her own residency at Cabrini-Green Homes in the spring 1981. But even prior to the mayor's move, the authority had voluntarily engaged the services of the firm of Ernst & Whiney to conduct an independent management study of CHA. That study was completed and released in May 1981, long before the Newman study began, and many of its recommendations have already been implemented.

What is troubling about the Newman report is that it carefully and deliberately avoids any recognition of significant reforms made at the authority during this past year. In fact, all of the data Newman uses is from 1980 or earlier, and seems largely based on newspaper clippings.

I am, of course, personally offended at the way in which Newman proceeds in this matter, since he avoids recognition of the improvements instituted under my administration, while he implies my responsibility for problems he describes which arose before I became director.

So that you may understand what we have actually accomplished since June 26, 1981, allow me to summarize briefly.

One, the Chicago Housing Authority showed not only a balanced budget for the first time in 5 years, but a small surplus for fiscal year 1982.

Two, the Chicago Housing Authority reduced its total staff by approximately 500 positions since May 1981. A general hiring freeze, except for critical positions, is still in effect.

Three, while the Chicago Housing Authority is expensive to run, even Newman's data shows that other well run authorities, like New York City, are higher. With the substantial cost controls effected in 1981, the Chicago housing authority's PUM is actually declining in real dollar terms.

Four, the Chicago Housing Authority completed its first two formal written union contracts in its history, and created and filled a new classification called utility janitor, a semiskilled position to enhance CHA's maintenance services and cut costs tremendously.

Five, the authority reorganized and redirected its modernization program to meet its emergent and long-term rehabilitation needs. Unfortunately, HUD has been sitting on approval of this new program since November 30, 1981, but accuses us at the same time of being dilatory.

During the last 8 months, the authority has also taken strong measures in several other areas long of concern to us and our residents.

One, the tenant selection process has been reconstituted and reinvigorated, providing complete background profiles on all prospective tenants.

Two, the Chicago Police Department took full control for security from private security firms, by establishing a complete public housing division within the new gang suppression unit of the Chicago Police Department on December 7, 1981.

Three, the purchasing policies and practices of the authority, which were already judged as conforming to accepted business practice by Ernst & Whinney, are being even further modernized into a completely accountable purchasing, receiving, and inventory system through a new computer program now coming on line.

Four, new personnel in all areas of the authority's operations have been recruited and hired solely on the basis of merit, including over half of our local development managers.

Five, the internal reorganization recommended by the Ernst & Whinney report began the day after I became executive director.

The area of our greatest improvement during the past year has been with the budget. The authority began 1981 with an aggregate deficit of $33.5 million, with the expectation that that deficit would rise to $51 million by the end of 1981. The authority's deficit had been the result of several inadequacies in the performance funding system, which as you know is the formula by which PHA's have received their subsidies since 1975.

Among these inadequacies, as I am sure you have heard before, Mr. Chairman, are the following: A ceiling placed on the funding level in 1975 was already exceeded by CHA and several other authorities which have therefore been penalized every year since the formula was introduced. The inflation factor used in the formula has been consciously underestimated at least by 50 percent by HUD and OMB over the life of the system. Certain factors, such as development age, building structure, crime, and so forth, are not adequately considered in PFS. And finally, utility expenses allowed by PFS do not reflect current consumption levels or utility rates.

The Chicago Housing Authority, with other large PHA's, has been struggling with the PFS since its inception. Our point of view, I think, finally won with the ABT study of 1979, which confirmed the factors noted above and called for revisions to the funding formula. That study, incidentally, was funded by HUD.

Nevertheless, facing our deficit position in 1981, the authority took the severe necessary steps noted above to curb spending and to begin to reduce its growth. As I said, the authority not only achieved a balanced budget in 1981 for the first time in 5 years, but actually showed a residual balance of approximately $200,000.

Therefore, instead of a projected $51 million deficit, the authority actually decreased its deficit in 1981.

Services, especially maintenance services, have been affected. To offset this, however, the authority created a new job classification, utility janitor, a semiskilled position, to make up for the service gaps and eventually improve overall service to our residents. Of course, this has also made CHA very competitive with other PHA's in the ratio of maintenance workers to units.

CHA still has a way to go. For example, we still have severe problems in our elevator maintenance and rehab program that we are attempting to address now.

But the Chicago Housing Authority has fulfilled its public trust and improved itself substantially during the past year. Some of these changes should be described as revolutionary, yet the Newman study entirely disregards them, and instead dwells on cliches and old newspaper reports attacking individuals personally and holding back progress in order to denigrate subsidized housing in this country generally.

Let me turn at this time to the more general issues confronting all public housing authorities today.

In 1981, the Federal Government initially provided 85 percent of the funding for which PHA's were eligible until Congress approved a supplemental appropriation that would bring all authorities to 97½ percent of PFS. It turns out that even that figure is still in question, as Mr. Jones commented, and the supplemental appropriation has not as yet been released.

Under these circumstances, as you have heard from other members of this panel, it has been almost impossible to budget appropriately during the past year. In 1981, CHA received $8 million in modernization, CIAP, funds for emergency rehab needs. Our actual total need at CHA to bring all our structures back to original building standards is $221 million. The true modernization requirements of PHA's throughout the Nation have been consistently underfunded and remain so today.

For 1982 and 1983, public housing authorities are most concerned about the maintenance of PFS as the standard for funding. PFS has inadequacies, as I stated earlier, but at least it bears some relationship to the true needs of our authorities.

Unfortunately, even though we are 6 months into Federal fiscal year 1982, we still do not know what our budgets will be, even though Congress has already appropriated funds. We have also heard that when the fiscal year 1982 subsidy is released, it may be dispersed at 75 percent of the funds that are available. To my knowledge, that was not and is not the intent of Congress. We are also led to believe that our utility adjustment factor will be posted against 1981 funds rather than 1982 as appropriated by Congress. We are further concerned about a reduction in funds through a newly proposed consumption reduction factor that no one yet seems able to compute.

In the meantime, HUD has raised rents of all of our residents to 25 percent of income and intends to raise those rents further to 30 percent. Food stamps may also be computed in the future as income, and all other deductions are to be eliminated. Half of our families and elderly are on fixed incomes; 97 percent are at 80 percent or less of the area's median income. How will our residents live with these types of increases?

We are told that the 1983 recommendations for public housing will provide only 65 percent of our eligible funding level and that modernization funds will be used for the demolition of 5,000 units nationwide. No new housing will be built.

What is of greater concern is that HUD expects to fund its 1983 revisions out of recisions made in the 1982 budget. This is hardly a sound revenue source. And, of course, it makes us concerned again about 1982, at which we estimate current funding at about 80 percent of PFS.

Public housing authorities, therefore, have ample justification from the comments I have made this afternoon to feel threatened. Threatened, not simply with respect to their budgets but with regard to their very existence, with regard to their very ability to maintain operations during the coming year.

But as I indicated earlier, if the real issue at hand is the entire notion of subsidized housing, housing for those most in need, especially during hard economic times, then we need to put that debate where it belongs, in Congress. All of the authorities are, I believe, open to new funding methods and other possible types of management arrangements, such as private management, but the future of public housing needs to be discussed openly, frankly, and honestly in Congress before important decisions are made.

In the meantime, public housing, to which this Nation has made an enormous and continuing commitment, must be funded adequately to do the job it is given to do

People numbering 150,000 live in CHA, 40,000 units in over 1,000 buildings, currently valued at over $750 million, housing people who, because of market and economic conditions, basically have nowhere else to go. Public housing is a reality. We cannot simply or quietly walk away from it in the hope that it will take care of itself. It is our responsibility, yours as well as mine, as well as the administration's.

I sincerely wish to thank you, Mr. Chairman, for the time and for your consideration of this very important matter. Thank you.

Chairman GONZALEZ. Well, we wish to thank you very much for a very excellent presentation. I admire you very much, and congratulate you on your achievements since you have assumed the directorship, and lament very much that you did get a hatchet act in the form of the so-called Newman study.

There is no question about that. However, we can't get our hands as yet, anyway, on such a report. I understand that HUD doesn't have it, at least up until now it does not admit to having it, but has issued only a sort of a summary.

Are you aware if the report has formally been published?

Mr. MOONEY. The whole way in which the report has been distributed, Mr. Chairman, I think is, as I indicated, not only unfair but somewhat disgraceful. The best way at this point to get a copy of the report is to send $12 to the Better Government Association in Chicago, and they will be happy to forward it to you. We have not as yet at the Chicago Housing Authority received that report formally, although I understand that the report has been forwarded to the city of Chicago.

But as I say, the only way at this point that I have a copy of it, and I believe I have one in my office, and I will check when I get back, is that you can buy it through this particular organization that received it as a leak on its way to the Chicago Sun Times.

Chairman GONZALEZ. Well, that was a contracted study or survey, wasn't it?

Mr. MOONEY. Yes; it was.

Chairman GONZALEZ The question I had, if it were that vital and that important to select Chicago for the study, what happened to the Inspector General?

Mr. MOONEY. The way that the study was presented to us and to the mayor in Chicago last summer, shortly after I became director, was that it would be an attempt by HUD to assist us with our management problems, which, as I say, we of course admit. We assured the Secretary of our complete cooperation, and I have to say to you in all honesty we have given more than what was due to the study team as they came through. In fact, in many instances they helped to halt some of the other important projects that my staff had been working on, because we have attempted to cooperate with them.

However, at some point during the course of that study, it became quite apparent to us that the cooperation we were offering was decidedly one way, and it became further clear to us that the study was intended to criticize the Chicago Housing authority, personally attacking members of the board of commissioners and others associated with the authority, and in general, I think, to be used in Congress against public housing and subsidized housing in this country.

Chairman GONZALEZ. The political aspects, the members of the board are really political. That is a political branch. I know that people don't like to use the word "political," but it is a policymaking body, and that is political. So I imagine that what happened there was that Newman somehow or other decided to get involved in local politics. It sounds like it to me.

Mr. MOONEY. If you have read the Chicago Sun Times over the last week, I think you could see that he has become an outstanding member of the local political scene.

Chairman GONZALEZ. Thank you very much.

We will proceed with Mr. Cleveland, and thank him for his patience while we kind of diverted here.

Excuse me, Mr. Cleveland. I understand a Mr. Schuelke is with you.

STATEMENT OF ROY J. CLEVELAND, EXECUTIVE DIRECTOR, NAVAJO HOUSING AUTHORITY, WINDOW ROCK, NAVAJO NATION, ARIZ., ACCOMPANIED BY JOHN H. SCHUELKE, ATTORNEY

Mr. CLEVELAND. Yes, sir.

Good afternoon, Mr. Chairman. I would like to thank you and the members of the subcommittee for inviting me to this hearing. I also would like to have our entire statement and attachment be placed in the record. I will only read the statement for this hearing.

Chairman GONZALEZ. Without objection, so ordered.

Mr. CLEVELAND. Mr. Chairman and members of the subcommittee, my name is Roy J. Cleveland. I am executive director of the Navajo Housing Authority. I have with me our attorney, John H. Schuelke, to assist me in responding to any questions you may have about our housing program.

The Navajo Housing Authority is the largest Indian housing authority both in area and in population. The Navajo Indian Reservation is approximately the size of the State of West Virginia, with a population of 152,694 persons. The projected population for the year 1990 is 191,825.

The Navajo Housing Authority was charted during the calendar year 1963. Through the Department of Housing and Urban Development-assisted public housing programs, we have constructed and have occupied 2,525 individual dwelling units. We have 661 units under construction, and another 1,365 units in various stages of planning. We have applied for 942 more units which we are ready to construct if we receive the units.

The Bureau of Indian Affairs has determined that the current housing inventory on the Navajo Reservation is 25,825 housing units. Out of this number, only 7,537 are considered to be in standard condition. The remaining 18,288 units are in substandard condition. Many of these units are in a hazardous condition due to decaying roofs and walls and the lack of proper water and sanitary sewer facilities. The current immediate need on the Navajo Reservation is 10,519 new dwelling units.

The housing needs for all Indian communities are substantial. The delivery of new housing to Indian communities is an extremely complex and difficult task. Cultural, religious, and political factors often appear to conflict with existing housing assistance approaches. In addition, the remoteness of Indian communities and the topographic and climatologic conditions add to this complexity.

The unique status of Indian community land and the trust relationship between the recognized tribes and the Federal Government, while necessary to protect the Indian community, has tended to further restrict the funding availability for safe, decent, and sanitary housing in Indian communities.

Although HUD has over the past 18 years produced over 28,000 new Indian housing units, it is estimated that more than 60,000 additional units will be required to satisfy the housing needs.

Indian communities are at the mercy of the almost sole source of housing, the Federal Government. The housing delivery system in an Indian community involves the intermingling of three departments of the Federal Government, builders, developers, public finance sources, architects, and a number of others. It is estimated that the Indian housing authorities which use Federal development funds presently provide 90 to 100 percent of all the dwelling units for low-income, needy families residing on Indian reservations.

Indian housing authorities have relied solely on Federal public assistance since private lending institutions and private builders/developers rarely enter Indian communities to build because of the trust status of the reservation land.

We have been told that the administration proposes to eliminate funds for new Indian housing units for fiscal year 1982 and 1983 because of: One, high construction costs. Two, high tenant accounts receivable. Three, too slow a delivery system. Four, a HUD estimate that there are 14,000 to 15,000 units already in the pipeline. Five, the administration wants to develop program alternatives.

In regards to high construction costs, the Navajo Housing Authority has developed statistics, copies of which are attached hereto, from which you will note that the average cost for a three-bedroom dwelling is approximately $65,000. This amount includes dwelling construction cost with equipment together with site improvements, land, administrative and planning expenses. The amount cited by the administration is $175,750 for the average dwelling on the Indian Reservations.

They fail to point out that this amount includes the overhead of HUD, BIA, and IHS as well as the interest expense necessary to retire the indebtedness over a period of years. We believe that if all these costs were added to private housing, that private housing costs would be comparable to Indian housing costs.

The high tenant accounts receivable just does not apply to the Navajo Housing Authority. Our total delinquency for public rental was approximately 6 percent, and for mutual help 11.5 percent for fiscal year 1981.

The lengthy delivery time is caused more by Federal redtape requirements than Indian Housing Authorities. All of the Indian Housing Authorities in the State of New Mexico together with the Navajo submitted recommendations to the Interagency Task Force to Study Indian Housing, copies of which were delivered to HUD. This submittal is attached hereto for your information. HUD refers to 14,000 to 15,000 units of Indian housing being "in the pipeline".

We cannot accept this figure. We have, along with a number of other Indian Housing Authorities, requested new housing units on many occasions only to be refused. Recently, when pressed by several Indian Housing Authorities from New Mexico, HUD finally admitted that there were only 1,609 units in the pipeline for the entire Region IX of HUD. Region IX serves all of the Indian Housing Authorities in California, Nevada, Arizona, and New Mexico. If there are units in the pipeline, we would like these units delivered to us now.

The Navajo Housing Authority has, as recently as March 8, 1982, filed statements in opposition to the administration's proposal to not fund Indian housing for fiscal year 1982 and 1983. A copy of our statement is attached hereto for your information. The Navajo Tribal Council has adopted a resolution opposing the termination, a copy of which is attached hereto for your information. All of the Indian Housing Authorities in HUD's Region IX have adopted a resolution opposing the administration's proposal, a copy of which is attached hereto. Apparently no one is willing to listen.

Indians were left out of the public housing for 25 years. We are behind the public sector, yet when termination of new housing is proposed, the Indian is one of the first to be eliminated. Why? The Indian communities have the greatest need for new housing. We believe it is unfair and inequitable to eliminate new Indian housing.

The United States has a responsibility to the Indian people morally and by numerous treaties to supply housing to Indians. We have proven we can build new houses and efficiently manage the projects. There is no other program available to us. Housing programs have supplied jobs, business opportunities, and community development on our reservation. Our unemployment, using a conservative estimate, is in excess of 50 percent.

H.R. 5731 is a temporary stopgap by proposing 4,000 new units of Indian housing. But we need a long-range program to be developed for Indian housing. We suggest that Indian Housing Authorities be funded directly with accountability to only one Federal agency. This would address all the concerns of the administration and provide much needed housing now.

We would welcome an opportunity to be involved in developing such a program.

Again, Mr. Chairman, I want to thank you for the opportunity to be at this hearing.

In addition, there is one other comment that I would like to include in my statement. That is, previously it was recommended by the administration that as a temporary measure, some of the housing funds would be directed to water and sewer facilities. This was a temporary measure. The administration should not deobligate itself to use the funds for the 4,000 units for water and sewer facilities.

[Mr. Cleveland's prepared statement, with attachments, on behalf of the Navajo Housing Authority, follows:]

PREPARED STATEMENT OF THE NAVAJO HOUSING AUTHORITY

Mr. Chairman and members of the Subcommittee, my name is Roy J. Cleveland. I am the Executive Director of the Navajo Housing Authority. I have with me our attorney, John H. Schuelke, to assist me in responding to any questions you may have about our housing program.

The Navajo Housing Authority is the largest Indian Housing Authority both in area and population. The Navajo Indian Reservation is approximately the size of the State of West Virginia with a population of 152,694 persons. The projected population for the year 1990 is 191,825.

The Navajo Housing Authority was chartered during the calendar year 1963. Through the Department of Housing and Urban Development assisted public housing programs we have constructed and have occupied 2,525 individual dwelling units. We have 661 units under construction and another 1,365 units in various stages of planning. We have applied for 942 more units which we are ready to construct if we receive the units.

The Bureau of Indian Affairs has determined that the current housing inventory on the Navajo Reservation is 25,825 housing units. Of this number only 7,537 are considered to be in standard condition. The remaining 18,288 units are in substandard condition. Many of these units are in a hazardous condition due to decaying roofs and walls and the lack of proper water and sanitary sewer facilities. The current immediate need on the Navajo Reservation is for 10,519 new dwelling units.

Housing needs for all Indian communities are substantial.

The delivery of new housing to Indian communities is an extremely complex and difficult task. Cultural, religious and political factors often appear to conflict with existing housing assistance approaches. In addition, the remoteness of Indian communities and the topographic and climatologic conditions add to this complexity. The unique status of Indian community land and the trust relationship between recognized tribes and the Federal government, while necessary to protect the Indian community, has tended to further restrict the funding availability for safe, decent and sanitary housing in Indian communities. Although HUD has over the past 18 years produced over 28,000 new Indian Housing units, it is estimated that more than 60,000 additional units will be required to satisfy the housing need.

Indian communities are at the mercy of the almost sole source of housing---the Federal government. The housing delivery system in an Indian community involves the intermingling of three departments of the Federal government, builders/developers, public finance sources, architects and a number of others. It is estimated that Indian Housing Authorities which use Federal development funds presently provide 90 to 100 percent of all the dwelling units for low income needy families residing on Indian Reservations.

Indian Housing Authorities have relied solely on Federal public assistance since private lending institutions and private builders/developers rarely enter Indian communities to build because of the trust status of the reservation lands.

We have been told that the Administration proposes to eliminate funds for new Indian Housing units for FY 82 and 1983 because

(1) high construction costs, (2) high tenant accounts receivable, (3) to slow a delivery system, (4) a HUD estimate that there are 14 to 15,000 units already "in the pipeline", and (5) the Administration wants to develop program alternatives.

In regard to high construction costs, the Navajo Housing Authority has developed statistics, copies of which are attached hereto, from which you will note that the average cost for a three bedroom dwelling is approximately $65,000. This amount includes the dwelling construction cost with equipment together with site improvements, land, administrative and planning expenses. The amount cited by the Administration is $175,750 for the average dwelling on Indian Reservations. They fail to point out that this amount includes the overhead of HUD, BIA and IHS as well as the interest expense necessary to retire the indebtedness over a period of years. We believe that if all of these costs were added to private housing that private housing costs would be comparable to Indian housing costs.

The high tenant accounts receivable just does not apply to the Navajo Housing Authority. Our total delinquecy for public rental was approximately 6 percent and for mutual help 11.5 percent for FY 81.

The lengthy delivery time is caused more by Federal "red tape" requirements than Indian Housing Authorities. All of the Indian Housing Authorities in the State of New Mexico together with the Navajo submitted recommendations to the Inter-agency Task Force to Study Indian Housing copies of which were delivered to HUD. This submittal is attached hereto for you information.

HUD refers to 14 to 15,000 units of Indian Housing being "in the pipeline". We cannot accept this figure. We have along with a number of other Indian Housing Authorities requested new housing units on many occasions only to be refused. Recently when pressed by several Indian Housing Authorities from New Mexico HUD finally admitted that there were only 1609 units "in the pipeline" for the entire Region IX of HUD. Region IX services all of the Indian Housing Authorities in California, Nevada, Arizona and New Mexico. If there are units "in the pipeline" we would like these units delivered to us now.

The Navajo Housing Authority has as recently as March 8, 1982, filed statements in opposition to the Administration's proposal to not fund Indian Housing for FY 82 and 1983. A copy of our statement is attached hereto for your information. The Navajo Tribal Council has adopted a resolution opposing the termination, a copy of which is attached hereto for your information. All of the Indian Housing Authorities in HUD's Region IX has adopted a resolution opposing the Administration's proposal, a copy of which is attached hereto. Apparently no one is willing to listen.

Indians were left out of Public Housing for 25 years. We are behind the public sector yet when termination of new housing is proposed the Indian is one of the first to be eliminated. WHY? The Indian communities have the greatest need for new housing. We believe it is unfair and inequitable to eliminate new Indian housing. The United States has a responsibility to the Indian people morally and by numerous treaties to supply housing to Indians. We have proven we can build new houses and efficiently manage the projects. There is no other program available to us. Housing programs have supplied jobs, business opportunities and community development on our reservation. Our unemployment using a conservative estimate is in excess of 50 percent.

H.R. 5731 is a temporary stopgap by proposing 4,000 new units of Indian housing. But we need a long range program to be developed for Indian housing. We suggest that Indian Housing Authorities be funded directly with accountability to only one Federal agency. This would address all of the concerns of the Administration and provide much needed housing now. We would welcome an opportunity to be involved in developing such a program. Thank you.

Respectfully submitted,

The Navajo Housing Authority

By Roy J. Cleveland
Roy J. Cleveland
Executive Director

BLANK PAGE

BLANK PAGE

NAVAJO HOUSING AUTHORITY
ANALYSIS OF DWELLING UNIT COSTS FOR PROJECT NO. AZ 12-51
AS OF FEBRUARY, 1982

Project No. AZ 12-51   115 Mutual Help Dwelling Units

Locations: Kayenta, Dennehotso, Rough Rock, Many Farms, Indian Wells, Leupp (Arizona)

Bid Opening Date: September 23, 1980

Total Bid Amount	:	$6,582,549.00
Total Administrative & Planning Costs:		1,434,319.00
Total Project Costs	:	$8,016,868.00

3 Bedrooms - 59 Units @ 1,280 S.F. = 75,520 S.F. ÷ 158,016 S.F. = 47.8%
4 Bedrooms - 34 Units @ 1,415 S.F. = 48,110 S.F. ÷ 158,016 S.F. = 30.4%
5 Bedrooms - 22 Units @ 1,563 S.F. = 34,386 S.F. ÷ 158,016 S.F. = 21.8%
115 Units   158,016 S.F.   100.0%

3 Bedrooms - 47.8% x $8,016,868 = $3,832,063 ÷ 75,520 S.F. = $50.74 Per S.F.
4 Bedrooms - 30.4% x 8,016,868 = 2,437,128 ÷ 48,110 S.F. = 50.66 Per S.F.
5 Bedrooms - 21.8% x 8,016,868 = 1,747,677 ÷ 34,386 S.F. = 50.83 Per S.F.

3 Bedrooms - 1,280 S.F. x $50.74 Per S.F. = $64,947 Per Unit Cost
4 Bedrooms - 1,415 S.F. x 50.66 Per S.F. = 71,684 Per Unit Cost
5 Bedrooms - 1,563 S.F. x 50.83 Per S.F. = 79,447 Per Unit Cost

NAVAJO HOUSING AUTHORITY
ANALYSIS OF DWELLING UNIT COSTS FOR PROJECT NO. NM 15-37
AS OF FEBRUARY, 1982

Project No. NM 15-37 88 Mutual Help Dwelling Units

Locations: Crownpoint, Tohatchi (New Mexico)

Bid Opening Date: September 23, 1980

Total Bid Amount : $5,044,998.00

Total Administrative & Planning Costs: 1,094,227.00

Total Project Costs : $6,139,225.00

3 Bedrooms - 45 Units @ 1,280 S.F. = 57,600 S.F. ÷ 120,665 S.F. = 47.8%

4 Bedrooms - 28 Units @ 1,415 S.F. = 39,620 S.F. ÷ 120,665 S.F. = 32.8%

5 Bedrooms - 15 Units @ 1,563 S.F. = 23,445 S.F. ÷ 120,665 S.F. = 19.4%

88 Units 120,665 S.F. 100.0%

3 Bedrooms-47.8% x $6,139,225 = $2,934,550 ÷ 57,600 S.F. = $50.95 Per S.F.

4 Bedrooms-32.8% x 6,139.225 = 2,013,666 ÷ 39,620 S.F. = 50.82 Per S.F.

5 Bedrooms-19.4% x 6,139,225 = 1,191,009 ÷ 23,445 S.F. = 50.80 Per S.F.

3 Bedrooms - 1,280 S.F. x $50.95 Per S.F. = $65,216 Per Unit Cost

4 Bedrooms - 1,415 S.F. x 50.82 Per S.F. = 71,910 Per Unit Cost

5 Bedrooms - 1,563 S.F. x 50,80 Per S.F. = 79,400 Per Unit Cost

NAVAJO HOUSING AUTHORITY
ANALYSIS OF DWELLING UNIT COSTS FOR PROJECT NO. AZ 12-62
AS OF FEBRUARY, 1982

Project No. AZ 12-62 130 Public Rental Dwelling Units

Locations: Kitsilee, Forest Lake, Nazlini, Chinle (2) (Arizona)

Bid Opening Date: September 25, 1981

Total Bid Amount :	$7,149,743.00
Total Administrative & Planning Costs:	1,761,237.00
Total Project Costs :	$8,910,980.00

1 Bedrooms - 6 Units @ 706 S.F. = 4,236 S.F. ÷ 148,792 S.F. = 2.8%
2 Bedrooms - 23 Units @ 872 S.F. = 20,256 S.F. ÷ 148,792 S.F. = 13.6%
3 Bedrooms - 59 Units @ 1,160 S.F. = 68,440 S.F. ÷ 148,792 S.F. = 46.0%
4 Bedrooms - 42 Units @ 1,330 S.F. = 55,860 S.F. ÷ 148,792 S.F. = 37.6%
130 Units 148,792 S.F. 100.0%

1 Bedrooms - 2.8% x $8,910,980 = $ 249,507 ÷ 4,236 S.F. = $58.90 Per S.F.
2 Bedrooms -13.6% x 8,910,980 = 1,211,893 ÷ 20,256 S.F. = 59.83 Per S.F.
3 Bedrooms -46.0% x 8,910,980 = 4,099,051 ÷ 68,440 S.F. = 59.89 Per S.F.
4 Bedrooms -37.6% x 8,910,980 = 3,350,529 ÷ 55,860 S.F. = 59.98 Per S.F.

1 Bedrooms - 706 S.F. x $58.90 Per S.F. = $41,583 Per Unit Cost
2 Bedrooms - 872 S.F. x 59.83 Per S.F. = 52,172 Per Unit Cost
3 Bedrooms -1,160 S.F. x 59.89 Per S.F. = 69,472 Per Unit Cost
4 Bedrooms -1,330 S.F. x 59.98 Per S.F. = 79,773 Per Unit Cost

NAVAJO HOUSING AUTHORITY
ANALYSIS OF DWELLING UNIT COSTS FOR PROJECT NO. NM 15-44
AS OF FEBRUARY, 1982

Project No. NM 15-44   20 Public Rental Dwelling Units

Location: Littlewater (New Mexico)

Bid Opening Date: September 25, 1981

Total Bid Amount	:	$ 971,967.00
Total Administrative & Planning Costs:		249,679.00
Total Project Costs	:	$1,221,646.00

2 Bedrooms - 4 Units @ 872 S.F. = 3,488 S.F. ÷ 23,068 S.F. = 15.1%

3 Bedrooms - 10 Units @ 1,160 S.F. = 11,600 S.F. ÷ 23,068 S.F. = 50.3%

4 Bedrooms 6 Units @ 1,330 S.F. = 7,980 S.F. ÷ 23,068 S.F. = 34.6%

20 Units 23,068 S.F. 100.0%

2 Bedrooms - 15.1% x $1,221,646 = $184,469 ÷ 3,488 S.F. = $52.89 Per S.F.

3 Bedrooms - 50.3% x 1,221,646 = 614,488 ÷ 11,600 S.F. = 52.97 Per S.F.

4 Bedrooms - 34.6% x 1,221,646 = 422,689 ÷ 7,980 S.F. = 52.97 Per S.F.

2 Bedrooms - 872 S.F. x $52.89 Per S.F. = $46,120 Per Unit Cost

3 Bedrooms - 1,160 S.F. x 52.97 Per S.F. = 61,445 Per Unit Cost

4 Bedrooms - 1,330 S.F. x 52.97 Per S.F. = 70,450 Per Unit Cost

November 13, 1981

INTER-AGENCY TASK FORCE TO
STUDY INDIAN HOUSING
Bureau of Indian Affairs
Department of Interior
Washington, D.C. 20240

Attn: The Honorable Kenneth Smith
Assistant Secretary

Gentlemen:

The following is a Position Statement of the NEW MEXICO INDIAN HOUSING AUTHORITIES.

The Department of Housing and Urban Development Public Housing Program for Indians is complex and difficult to deal with because of many factors. The apparent root of the problem is the guardian-ward relationship created by treaties between the United States and the various Indian Tribes and other laws, which causes difficulty in dealing with the land status for each particular Tribe.

The present Public Housing Program which is administered by the Department of Housing and Urban Development is the only effective Housing Program functioning on most of the Indian Reservations. Granted, the Program has problems and in the opinion of this group, certain areas definitely require improvement; however, the undersigned are all opposed to changing the Program from the Department of Housing and Urban Development to the Department of the Interior. The reasons are numerous, but the paramount reason is the concern that a change from one department of the Government to another will cause extensive delays in the Program. The undersigned believe that the better approach would be to continue the present Program under the Department of Housing and Urban Development, but make changes which would expedite delivery and lower the cost of housing to the various Tribes and the Government, as well. With this thought in mind, the undersigned would like to propose the following changes in the present Program which would reduce costs and delivery time:

1. The Inter-Departmental Agreement should be reviewed and refined to effect better coordination between the three federal agencies concerned with federal housing, and one agency, preferably HUD, should be designated as the agency having the lead role and authority to enforce compliance with the Inter-Departmental Agreement.

2. The HUD regulations should be changed to allow the re-use of drawings and plans, exchanged between the various Housing Authorities, without extensive HUD review, since the plans have already been approved. This would diminish the delivery time substantially.

3. There should be allowances made for remoteness in determining costs and delivery time.

4. A review of the Davis-Bacon wage rates should be conducted to determine if they are impacting the cost of Public Housing Programs.

5. An investigation and review of Indian contract preference should be conducted to determine if this is a factor in increased costs

and if it is impacting the delivery system of housing to the Housing Authorities. Tribes should have the option to choose Indian contract preference.

6. The Department of Labor should be included in an Inter-Departmental Agreement since labor is approximately 40% of the cost of housing programs and the Housing Authorities are required to comply with the Department of Labor requirements in apprenticeship training, affirmative action, and wage rates.

7. HUD should be authorized to grant administrative loans to Indian Housing Authorities for the purposes of pre-preliminary investigation of the sites, soils investigations, surveys, archaeological clearances, environmental assessments, etc., prior to issuing Program Reservations.

8. HUD should consider implementation of a lease-purchase program for the Indian housing rental units. This has been proposed on numerous occasions by Indian Housing Authorities, but never implemented.

9. HUD should consider post-bid negotiations with the lowest responsible bidder for conventional construction of the projects, and also allow for the use of alternate bidding (additive or deductive).

10. HUD should be required to delegate approval authority to the Field Offices, such as in Phoenix and Albuquerque.

11. HUD should consider the granting of more latitude in the application of Minimum Property Standards to consider the differences

in climatic conditions, soils conditions, etc., on the various Reservations.

12. HUD should proceed immediately to an Annual Contributions Contract after Program Reservation to curb inflationary factors which are involved in the present Program between Program Reservation and final signing of the Annual Contributions Contract.

13. Establish higher less-restrictive threshholds for archaeological and environmental clearances, such as waiver for housing projects of less than 200 units. Approvals by several Government agencies are unnecessary, and clearance by one agency should be sufficient.

14. HUD should grant incentives to Indian Tribes and Housing Authorities who have shown they can deliver the housing within the costs and are effecting rent collections by granting the particular Authority new housing units. This means, why penalize one Indian Tribe or region for the inefficiency of another region?

15. HUD should change the present approach to determining operating subsidies such that maintenance and rehabilitation costs should be reflected in the operating subsidy for management of the projects.

16. A fast track system for technical review process should be established in HUD. For example, an architect's work which has been previously acceptable to HUD should not require such a lengthy review as a new architect's. An architect who is using plans that have been

approved before should not be subjected to the same lengthy technical review. Such reviews should be conducted at the field offices rather than the Regions. Reviews should be completed within mandated time periods.

17. The position of Special Advisor to the Secretary of HUD for Indian Housing should be filled in Washington, and that person should be given authority and responsibility to effect more efficient delivery systems of public housing to the Indian Tribes.

Respectfully submitted,

NAVAJO HOUSING AUTHORITY

By

JICARILLA APACHE HOUSING AUTHORITY

By Cassandra Medina

ALL INDIAN PUEBLO HOUSING AUTHORITY

By

MESCALERO APACHE HOUSING AUTHORITY

By

NORTHERN PUEBLOS HOUSING AUTHORITY

By

PUEBLO OF LAGUNA HOUSING AUTHORITY

By

Project Office
P O Box 348
Tuba City AZ 86045

Project Office
P O Box 586
Kayenta AZ 86033

Project Office
P O Box 427
Chinle AZ 86503

Project Office
P O Box 880
Shiprock NM 87420

Project Office
P O Box 97
Tohatchi NM 87325

Project Office
P O 764
Fruitland NM 87416

Project Office
P O Box 137
Navajo NM 87328

Project Office
P O Box 597
Ft Defiance AZ 86504

Project Office
P O Box 187
Crownpoint NM 87313

Navajo Housing Authority
Position Statement
Opposing Rescission of 4,000 Dwelling Units and Termination of Indian Housing Programs

March 8, 1982

P.O. BOX 387 Window Rock, Navajo Nation, Arizona 86515 Phone: (602) 871-4114

Why rescind funding for new Indian Housing units for Fiscal Year 1982? Why is new Indian Housing funding omitted from the Fiscal Year 1983 Budget? These questions require an immediate answer.

The performance of the United States with respect to Indian Housing is most disappointing. Historically the United States Congress by the Housing Act of 1937 commenced low income public housing programs for all qualified American citizens EXCEPT American Indians. The Department of Housing and Urban Development (HUD) was the Department designated to administer the program. American Indians were not included in public housing programs until 1962, twenty-five years later.

When American Indians were finally included in public housing programs, it was determined that the per capita need for decent, safe and sanitary housing was greatest among the Indian people. HUD was the governmental agency chosen to manage Indian housing programs.

Has the need for new Indian housing been satisfied? No. The Comptroller General's Report to the Congress of the United States of March 31, 1978, emphasized that substandard Indian housing increased despite federal efforts and recommended that Congress redefine the national policy for Indian housing and establish a centrally administered program with realistic goals and objectives. Indian leaders were not consulted as to changes to improve the Indian housing programs.

The HUD Annual Report to Congress FY 1979 expressed high concern over delivery cost of Indian housing. Even after this report, Indian leaders were not asked to recommend changes for improvement of the program. Now the Reagan Administration has rescinded funding, in effect, terminating new Indian housing.

We would like it clearly understood that Indians are greatly concerned about the termination of funding for Indian housing. Indian Housing Authorities in New Mexico, Arizona, Nevada, and California have reacted strongly against the proposed funding cuts. A resolution was adopted by all the New Mexico Indian Housing Authorities opposing the proposed zero funding and making recommendations to improve the program. The Indian Housing Authorities in all four states, in a joint resolution, opposed the funding cuts. The Navajo Tribal Council has adopted a resolution in opposition to the funding cuts. Copies of these documents are attached for the information of readers of this statement.

We understand there is a bill proposed which would move Indian housing from HUD to the Department of the Interior. Why are we not asked for our thoughts and recommendations? Again, we are just moved around without even the courtesy of telling us before introducting legislation.

We have suggestions and recommendations to save money. We are a large housing authority which has established a successful tract record in housing. Why not remove all red tape?

Fund the Navajo Housing Authority directly. We can build our own houses. We don't need the BIA, IHS or HUD. This would lower the cost of our housing and substantially shorten the delivery time. We have demonstrated the Navajo ability to build houses and administer housing programs.

The Treaty of 1868 between the United States and the Navajo Tribe of Indians contained promises by the United States to provide for the health, education and well-being of the Navajo people. All can agree that a decent, safe and sanitary dwelling is included in these promises.

We believe the United States has failed to carry out its commitments. The Congress left Indians out of public housing programs for a quarter of a century. Now Indian housing is to be one of the first programs to be terminated.

Our government appears to be more concerned about foreign countries than its own people. Billions of dollars of foreign aid are sent from our country every year all over the world. Why can't our people come first? We are taxpayers and citizens of this country. We believe priorities should be re-evaluated. Take care of our American people's needs first and if there is a surplus, then send aid to foreign countries.

Many groups profess to represent the Indians. Because of numerous groups making representations on behalf of the Navajo Nation, the Navajo Tribal Council has passed a resolution which allows only authorized representatives of the Navajo Tribal Government to speak for the Navajo Nation. This position statement is submitted on behalf of the Navajo Nation.

We respectfully request answers to our questions of why rescind funding for new Indian housing units for FY 1982 and why is funding for construction of Indian housing omitted from the FY 1983 budget? Is Congress abdicating its responsibility and treaty obligations to the Navajo Nation? Why not fund the Navajo housing program separate from other Indian housing?

Your response will be sincerely appreciated.

Respectfully submitted,

NAVAJO HOUSING AUTHORITY

James T. Nahkai, Jr.
Chairman
Board of Commissioners

BEST DOCUMENT AVAILABLE

CF-16-82

Class "C" Resolution
No BIA Action Required.

RESOLUTION OF THE
NAVAJO TRIBAL COUNCIL

Opposing the Termination or Transfer of the
Department of Housing and Urban Development
Administered Indian Housing Programs

WHEREAS:

1. The Navajo Tribal Council chartered the Navajo Housing Authority as a non-profit public agency during the calendar year 1963 to enable the Navajo Tribe of Indians to participate in low-income public housing programs administered and funded by the Department of Housing and Urban Development; and

2. The Navajo Housing Authority has constructed 2,636 dwelling units throughout the Navajo Nation which provide decent, safe and sanitary housing for approximately 13,000 people who previously resided in substandard housing; and

3. The Navajo Housing Authority has under construction 452 dwelling units which will house 2,200 Navajo people with an additional 1,330 units in the design stages which will ultimately house 6,600 more people; and

4. The Navajo Housing Authority program is presently providing much needed decent, safe and sanitary housing on the Navajo Nation; and

5. Recent Bureau of Indian Affairs' surveys have revealed that there are 18,288 dwelling units on the Navajo Reservation in substandard condition, 12,243 of which need immediate renovation work, while 10,519 new dwelling units are needed; and

6. The Fiscal Year 1983 Reagan Administration Budget proposes no new funding for Indian housing programs; and

7. The Bureau of Indian Affairs is seeking to have the Department of Housing and Urban Development Indian housing programs transferred to the Bureau of Indian Affairs; and

8. The Navajo Housing Authority submitted a position statement June 29, 1981, opposing termination of Department of Housing and Urban Development Indian housing programs, to numerous Congressional delegates and committees; and

9. The Navajo Housing Authority, with other New Mexico Housing Authorities, has submitted a letter (Exhibit "A" attached hereto) dated November 18, 1981, to the Inter-Agency Task Force to Study Indian Housing with recommended changes which could expedite delivery and lower the costs of housing to the various tribes and governments; and

10. The Navajo Tribal Council believes it is in the best interest of the Navajo Nation for the present Department of Housing and Urban Development Indian housing programs to continue with appropriation modifications to improve the program as suggested in the letter of November 18, 1981, noted above; however, rather than terminate the program the Navajo Nation should concur with the transfer of the housing program to another federal agency.

NOW THEREFORE BE IT RESOLVED THAT:

1. The Navajo Tribal Council hereby strongly opposes the termination of the Indian housing programs presently funded and administered by the Department of Housing and Urban Development.

2. The Navajo Tribal Council further opposes the transfer of the Indian housing programs from the Department of Housing and Urban Development to the Bureau of Indian Affairs and favors the modifications of existing programs, as recommended in Exhibit "A" attached hereto, or in the alternative, approves the transfer of the housing programs to a federal agency other than the Bureau of Indian Affairs, if it would mean continuation of the programs.

3. The Navajo Tribal Council opposes the Block Grant concept where Indian housing funds would be remitted to the several states for transmittal to the Indian tribes.

4. The Chairman, Navajo Tribal Council, is authorized and directed to present this resolution to President Ronald Reagan and all others he deems appropriate to contact for the best interest of the Navajo Nation.

CERTIFICATION

I hereby certify that the foregoing resolution was duly considered by the Navajo Tribal Council at a duly called meeting at Window Rock, Navajo Nation (Arizona), at which a quorum was present and that same was passed by a vote of 68 in favor and 0 opposed, this 11th day of February, 1982.

Vice Chairman
Navajo Tribal Council

RESOLUTION OF INDIAN HOUSING AUTHORITY IN THE STATES OF CALIFORNIA, NEVADA, ARIZONA AND NEW MEXICO

WHEREAS:

1. HUD, through its Region IX office provides funding and administrative assistance to Indian Housing Authorities located in the States of California, Nevada, Arizona and New Mexico; and

2. It is understood that funding for new Indian housing dwelling units may be interrupted or terminated; and

3. The Federal Government has special obligations to Indian people to provide safe, decent and sanitary housing as has been furnished through the HUD Indian Housing Programs for approximately 20 years; to abdicate this responsibility would be a breach of its leagal and moral obligation to Indian people; and

4. The consequences of such proposed action would have such drastic and far reaching effects that this group is compelled to state its position and made alternate recommendations to improve and continue the program furnishing much needed housing to Indian people.

BE IT RESOLVED THAT:

1. All of the Indian Housing Authorities in California, Nevada, Arizona and New Mexico demand the continuation of the Indian Housing Program with funding at a level to meet the Federal Government's legal and moral responsibilities to Indian people.

2. Housing Programs for Indian people be expanded so all Indian people could participate in different Federal housing programs just as their non-Indian counterparts.

3. The Federal Government involve representative Indian people in reformulating Indian Housing Programs to reduce the cost and speed the delivery of Indian housing.

4. It is recommended that the duty to provide Indian housing remain the responsibility of HUD.

5. This resolution be delivered to administration officials, Congressional delegations of the four states and other persons involved with Indian housing.

6. Roy J. Cleveland sign as Chairman and Wayne Chico as Secretary of the meeting on the certification of this resolution.

CERTIFICATION

We hereby certify that the foregoing resolution was duly considered and adopted by the Indian Housing Authorities of California, Nevada, Arizona and New Mexico at a duly called meeting at Phoenix, Arizona, on the 13th day of January, 1982.

Roy J. Clevel
Chairman

Attest:

Wayne C.
Secretary

Chairman **Gonzalez**. Yes, I am very much aware of that, because I was the only one on the floor when the appropriation for the Interior came up, and I fought that.

I am going to have to recess for about 25 to 50 minutes, and resume at the end of that time.

[Whereupon, a brief recess was taken.]

Chairman **Gonzalez**. The subcommittee will resume.

Mr. Cleveland and Mr. Schuelke, again thank you for being patient. We apologize profusely. There is not much we can do. We had one of those unusual things. This has not happened in quite some time.

Well, let me just comment generally that we have been extremely concerned, and of course the very sorry record and now the administration's hard-heartedness is very difficult to understand. And I think you realize that our bill, which is what we are traveling on in these hearings, 5731, is really sort of a survival bill. It is not what I would present if it were just me asking, but it is just a barebones survival bill, and particularly in the case of Indian housing.

And there is nobody that is more conscious of the fact that we ought to have some single-agency responsibility than I am. And I think the majority of the Members, at least on the majority side, are very well aware what are the housing needs of the Indian communities in our country. Unfortunately this is not generally true of the majority of the Members of the House, or for that matter the Senate.

But I will be very frank with you. I never thought that I would see the day, while serving in the Congress, that such a wholesale abdication of a responsibility or a commitment that Congress has made to Indian Tribes, belatedly in the case of Indian housing, true, as proposed by this administration.

HUD is proposing soon to establish the minimum rents for public housing tenants equal to the cost of utilities. I was thinking during your presentation, if the administration is sincerely interested in vacating in favor of, say, private enterprise in the case of public housing or the States in the case of general Federal programs and policies, such as advocated in the New Federalism, I want to know how it is going to privatize Indian housing.

I mean, what capacity is there without Federal assistance? And of course, I agree with the statement made by Mr. McCauley and one or two of the other witnesses that clearly impugn the motives of the administration. After 1 year and 1 month as of the date of the last appearance of the Secretary of HUD, I am firmly convinced that the administration is intending to kill off the programs, not have them last even to give them to the States.

And in the case of Indian housing, there is no question that they are zeroing it out in the budget recommendations, which clearly shows that they have made a decision that they are not going to be for Indian housing. But how in the world could this program be privatized?

Mr. **Cleveland**. Mr. Chairman, I do not see any possibility of a private enterprise to come on a reservation and try to develop housing, especially the low-income housing. We have stated in our report that the land status has a great deal to do with the private or anybody coming on the reservation, developing housing or communities. The way the land is structured, you cannot put a lien on the land. So it would make it virtually almost impossible.

You probably could use some other type of collateral, but generally they would like real estate in their dealings. So therefore, private industry would have a very difficult time, if not impossible, in developing housing, like I said, especially low-income housing on the reservations.

And a lot of the people that are on the reservation do not have the income to service the debt. And the way our economy is right now, we use the 50 percent figure, in excess of 50 percent, but our unemployment rate is a lot higher than that.

So how can we, if there is no money, if there is no employment, how do we get people to have housing or pay for housing?

Chairman **Gonzalez**. Well, there are some of us here who are pledged to the commitment and we will continue.

We do have the situation where we have two other witnesses that have been waiting very patiently, and one of them does have an emergency situation with respect to catching a plane. But I did not want to dismiss the panel unless we give an opportunity to Mr. Schuelke, in case you have some statement to make or a question to raise. I think we should recognize you. You have come all the way here and we appreciate it.

Mr. **Schuelke**. Thank you, Mr. Chairman. I do not have any particular statement. However, we are concerned about a possibility of losing our housing entirely, which appears to be on the horizon. And we believe that Congressman Udall is presently proposing to sponsor legislation which would in effect transfer the housing responsibility from HUD to the Bureau of Indian Affairs.

We have not had an opportunity to analyze the bill. However, we are very concerned that in any such transition there is a delay in implementing a program to the extent that we may be without housing for 1 year or longer. And we would like you to know that such legislation is apparently going to be proposed.

Chairman **Gonzalez**. I appreciate that.

Mr. **Schuelke**. But our concern is, we just do not feel that our program can be interrupted. We are 25 years behind now and if it is interrupted any further it probably will die.

Chairman **Gonzalez**. I really appreciate you informing me, because I have had no communication from Mr. Udall, not at this point. I think we had some last year, but that was with respect to the continuing resolution on appropriations for the Department of the Interior, the Subcommittee on Appropriations. Sid Yates brought the matter up, and even there they had no communication with me.

It just so happens I made it a point to be there on the House floor and raised the issue on the record two times last year. So I do not know, but you know, being informed is half the battle won. And I will anticipate and make sure that I contact Mo Udall, a very good friend, and find out exactly what his intentions are and if he has prepared the bill and will get a copy of it. So we will be looking for it.

Mr. **Schuelke**. We would certainly appreciate that, Mr. Chairman.

And we understand that your bill is a temporary measure. We would really appreciate it.

Chairman **Gonzalez**. It is a lifeline. In your statement you assessed it correctly that it does not address itself to the fundamental problem. I will grant that, but this is just a survival.

Mr. **Schuelke**. We certainly appreciate that, Mr. Chairman. Thank you.

Chairman **Gonzalez**. Thank you very much, and thank you for taking your time and being with us. We will continue to be, as our staffs have been with yours, in communication with you.

Mr. **Cleveland**. Thank you, Mr. Chairman.

Chairman **Gonzalez**. We now wish to recognize Mr. Robert E. Esrey, the president of the National Apartment Association, and Mr. Ron Shiffman, the director of the Pratt Institute, New York City, Center for Community and Environmental Development.

Let me say right at the outset that I apologize for all of this delay and thank you for your patience. And I am also aware that you have a problem with respect to catching a plane. So we will recognize you right away, Mr. Esrey.

STATEMENT OF ROBERT E. ESREY, PRESIDENT, NATIONAL APARTMENT ASSOCIATION, ACCOMPANIED BY SCOTT SLESINGER, GENERAL COUNSEL

Mr. **Esrey**. I am very appreciative, Mr. Chairman. I know the delay was not of your doing.

Good afternoon to you, sir, and members of the subcommittee. My name is Robert Esrey and I am president of Robert E. Esrey & Co., an income property management firm in Kansas City, Mo. As president of the National Apartment Association, I am testifying today on behalf of our membership, which includes over 45,000 owners, developers, and managers of multifamily housing throughout the Nation. The NAA is a trade association exclusively representing the multifamily housing industry.

Accompanying me today is our general counsel, Scott Slesinger.

Mr. Chairman, I request that my statement be printed in the record, which I will read.

Chairman **Gonzalez**. Without objection, so ordered.

Mr. **Esrey**. Thank you, Mr. Chairman.

Before I begin my discussion of H.R. 5731, the Housing and Community Development Amendments of 1982, and H.R. 5568, the Home Mortgage Capital Stability Act, I would like to present a general overview of the state of the rental housing market in our great Nation.

Nationally, the vacancy rate stands at a record low of 5 percent. However, the rental market varies considerably across the country. Last year, 1 out of every 8 unsubsidized rental starts were in Houston, Tex., where vacancies were held below 5 percent. Minneapolis, Minn., Dallas, Tex., and Phoenix, Ariz., also have had considerable construction and continue to have low vacancy rates. On the other hand, according to Advance Mortgage Corp., Washington, D.C., Boston, Mass., and Atlanta, Ga., usually tight rental markets, are experiencing growing vacancy rates due to the doubling up of unrelated persons.

Some rental residents no longer see homeownership as the ultimate hedge against inflation—a view espoused now by some economists. Variable interest rate mortgages have contributed to an increase in the risks and liabilities in homeownership that were absent a few short years ago. Thus, the demand for rental housing is increasing. In some areas, this means a need for new construction; in other areas, it means an increase in young adults moving back home or resorting to doubling-up.

Total multifamily rental starts for 1981 totaled approximately 174,000 units nationwide. Of those, approximately two-thirds were government-assisted. The high costs of labor and materials, in conjunction with potentially more profitable investments elsewhere, have discouraged new, unsubsidized rental construction.

However, the single most significant factor today is that in none but the most exceptional community can a developer build in the present interest rate climate unless investors commit considerable equity, sometimes as high as 50 percent. In many areas, developers cannot build affordable units and carry the interest charges, so they must wait on the sidelines.

The tightening of the market has allowed rents to increase. During the inflationary 1970's, the price of a single-family home increased 194 percent, outpacing the increase in the Consumer Price Index for all goods and services. On the other hand, rents increased at an average of only 5.3 percent per year or about half that of homeownership.

With inflation moderating, 1981 was the first year since 1977 that the CPI for rents almost equalled that for all goods and services. Despite the comparable moderation of rent increases, many governments, in the face of a dwindling supply of housing and increased tenant demands for assistance, have imposed limits on the rents that can be charged by owners.

Numerous studies have shown that the impact of rent control on rental housing is counterproductive. Investors simply will not invest in rental housing, but would rather use their funds in other investment opportunities which do not have profit ceilings. Meanwhile, present owners in rent-controlled communities, unable to make a fair profit, look to convert their units to condominiums, further decreasing the amount of rental stock.

Every study shows that when an owner's income is kept artificially low by rent control, maintenance is the first expense to be deferred, leading to a deterioration of the housing stock, a situation most dramatically shown in New York. As rents are held below the required return, the controlled units are reassessed for real estate tax purposes, limiting the city's ability to serve its constituents or, more likely, shifting the tax burden onto homeowners.

Rent control, or even the fear of rent control, makes all but the most speculative investors avoid the rental market.

Mr. Chairman, national legislation, much of which originated in this room, has made this the best-housed country in the world. The thrift institutions' link to housing, the long-term level payment FHA mortgage, rental construction for the poor, local grants for housing infrastructure, and the homeownership interest deduction have significantly improved the housing available to our citizens.

The important remaining problem is making housing affordable to the poor. We believe the new depreciation schedules, minor changes in the tax-exempt bond legislation, and lowered interest rates will make it possible for the Federal Government to limit its direct efforts in construction housing for the poor. However, a program will be necessary to make housing affordable for those families who cannot afford market rents. The President's Commission on Housing and the administration are clearly moving in that direction, based on the success of the section 8 existing program.

We believe a rental assistance voucher could work. However, several serious problems exist with the proposal presented thus far by the administration. If the assistance is sufficient to make the poor true consumers in the rental market and if the volume of persons served by the program is large enough to make those eligible a force in the marketplace, I am confident that the private sector will provide efficient, quality units.

Mr. Chairman, the private market cannot support all the needed housing, especially in this time of high interest rates. Therefore, we strongly support funding for section 8 projects that have commitments. As you know, many developers have in good faith spent considerable funds based on the section 8 commitments they hold. However, the administration proposes to rescind those commitments already in the pipeline for projects that are unable to receive affordable financing.

We endorse section 205 of the bill that would continue the GNMA tandem program. We note that last year the administration did support funding of the GNMA pipeline. Such a move will increase both employment and the rental housing supply faster than any other program this committee could support.

We applaud the introduction of your housing construction program, which is targeted to communities that are most in need. Your approach wisely avoids the multiyear commitment problem that doomed the section 8 construction program. The targeting provision could be advantageous in constructing housing where the conventional market is unable to meet the housing demand. We offer two suggestions:

One, the subsidy required to construct and amortize the debt on rental housing is very high, especially if labor rates are excessive. Section 318 of the bill requires that Davis-Bacon rates be paid to workers on projects financed under this bill. There is no question that Davis-Bacon forces wages up to the point that units built for the poor are sometimes the most expensive units in the area.

By deleting that section of the bill, significantly more units can be built with the same dollars. At a time when there is a serious need for this housing and when unemployment is high, it is unconscionable to waste precious Federal resources by requiring that already highly paid construction workers in federally assisted housing projects receive higher wages than those in non-federally assisted projects. In addition, the present apprenticeship provision discriminates against younger workers, women and minorities. Clearly, Davis-Bacon has outlived its usefulness.

Two, section 313 defines the area eligibility criteria. The aim is to target where subsidized construction is most needed. Unfortunately, the criteria, such as the duration of rental housing vacancies and the extent of rental housing production lag, in many cases define the direct effect of rent control.

We believe it is wrong to reward localities which, through local ordinances such as rent control, created their own housing problems. Such communities do not deserve to be targeted. A better use of scarce Federal dollars is to help those communities trying to grapple with and realistically solve their rental housing problems.

Mr. Chairman, we would also like to say a few words about H.R. 5568, introduced by Mr. St Germain. The thrift institutions are clearly in serious trouble and the cost of saving them will be tremendous if interest rates do not moderate. Savings and loans and mutual savings banks hold over $55 billion in multifamily mortgages. Mutual savings banks, which are limited primarily to the Northeast, hold a greater volume of such mortgages than all the commercial banks in the country.

Our association, while taking no position on particular legislation affecting savings and loans, urges this body and the administration to ease the fears held by many that a run on the thrifts could occur, leading to a collapse of confidence in all financial institutions. Whatever is done, the public must be convinced that their savings deposits are safe.

The caption to H.R. 5568 cites another important reason to save the thrifts—"to insure the availability of financing for housing." Rental property is a good investment for the thrifts. However, the value of any real estate security is a factor of the income the property can generate.

Any local ordinance, or even the threat of one, that would limit the possible earnings of the property eliminates prudent investors. Such laws imperil the institution and increase the exposure of insurance funds which back regulated lenders. At a minimum, it causes the risk to substantially increase, so lenders raise the interest rate. This increases the cost of the project, requiring the rent to also increase, making units less affordable.

We want and need thrifts to invest in multifamily housing. To do so requires some assurance that their investment is safe. Therefore, we urge that an amendment be passed providing that any project financed by a loan from a federally insured institution be exempt from rent control. This proposal has the endorsement of the President's Housing Commission.

Such an amendment would protect the lending institutions, the Federal Government through its depository insurance agencies, and will lead to the construction of multifamily housing. The alternative is that nonsubsidized rental housing will not be built, even when interest rates decline, in communities with rent control or the threat of rent control.

Governments will then be asked to provide the needed supply. At a time of limited Federal funds for construction, freeing private enterprise to build units would be a most cost effective program.

This concludes my statement. Thank you for the opportunity to express the views of the National Apartment Association, and I will be happy to try to answer any questions you may have.

[Mr. Esrey's prepared statement, on behalf of the National Apartment Association, follows:]

PREPARED STATEMENT OF ROBERT E. ESREY, PRESIDENT, NATIONAL APARTMENT ASSOCIATION

Mr. Chairman and Members of the Committee:

My name is Robert Esrey, and I am President of Robert E. Esrey and Company, an income property firm in Kansas City, Missouri. As President of the National Apartment Association, I am testifying today on behalf of our membership, which includes over 45,000 owners, developers, and managers of multifamily housing throughout the nation. The NAA is a trade association exclusively representing the multifamily housing industry. Accompanying me today is our General Counsel, Scott Slesinger.

Mr. Chairman, before I begin my discussion of H.R. 5731, "The Housing and Community Development Amendments of 1982," and H.R. 5568, "The Home Mortgage Capital Stability Fund," I would like to present a general overview of the state of the rental housing market in our great nation.

Nationally, the vacancy rate stands at a record-low of 5%. However, the rental market varies considerably across the country. Last year, one out of every eight unsubsidized rental starts was is Houston, Texas, where vacancies held below 5%. Minneapolis, Minnesota; Dallas, Texas; and Phoenix, Arizona also have had considerable construction and continue to have low vacancy rates. On the other hand, according to Advance Mortgage Corporation, Washington, D.C.; Boston, Massachusetts; and Atlanta, Georgia, usually tight rental markets, are experiencing growing vacancy rates due to the "doubling-up" of unrelated persons. Some rental residents no longer see homeownership as the ultimate hedge against inflation--a view espoused now by some economists. Variable interest rate mortgages have contributed to an increase in the risks and liabilities in homeownership that were absent a few short years ago. Thus, the demand for rental housing is increasing. In some areas, this means a need for new construction; in other areas, it means an increase in young adults moving back home or resorting to "doubling-up."

Total multifamily rental starts for 1981 totaled approximately 174,000 units nationwide. Of those, approximately two-thirds were government assisted. The high costs of labor and materials, in conjunction with potentially more profitable investments elsewhere, have discouraged new rental construction. However, the single most significant factor today is that in none but the most exceptional community, can a developer build in the present interest rate climate unless investors commit considerable equity--as high as 50%. In many areas, developers cannot build affordable units and carry the interest charges, so they must wait on the sidelines.

The tightening of the market has allowed rents to increase. During the inflationary 1970's, the price of a single family home increased 194%, outpacing the increase in the Consumer Price Index (CPI) for all goods and services. On the other hand, rents increased at an average of only 5.3%, or about half that of homeownership. With inflation moderating, 1981 was the first year since 1977 that the CPI for rents almost equalled that for all goods and services. Despite the comparable moderation in rent increases, many governments, in the face of a dwindling supply of housing and increased tenant demands for assistance, have imposed limits on the rents that can be charged by owners. Numerous studies have shown that the impact of rent control on rental housing is counterproductive. Investors will simply not invest in rental housing, but will rather use their funds in other investment opportunities which do not have profit ceilings. Meanwhile, present owners in rent controlled communities, unable to make a fair profit, look to convert their units to condominiums, further decreasing the amount of rental stock. Every study shows that when an owner's income is kept artificially low by rent control, maintenance is the first expense to be deferred, leading to a deterioration of the housing stock, a situation shown most dramatically in New York and Paris. As rents are held below the required return, the controlled units are reassessed for real estate tax purposes, limiting the city's ability to serve its constituents or more likely shifting the tax burden onto homeowners. Rent control, or even the fear of rent control, makes all but the most speculative investors avoid the rental market.

Mr. Chairman, national legislation, much of which originated in this room, has made this the best housed country in the world. The thrift institution's link to housing, the long-term level payment FHA mortgage, rental construction for the poor, local grants for housing infrastructure, and the homeownership interest deduction have significantly improved the housing available to our citizens. The important remaining problem is making housing affordable to the poor. We believe the new depreciation schedules, minor changes in the tax-exempt bond legislation, and lowered interest rates will make it possible for the federal government to limit its direct efforts in construction housing for the poor. However, a program will be necessary to make housing affordable for those families who cannot afford market rents. The President's Commission on Housing and the Administration are clearly moving in that direction based on the success of the Section 8 existing program.

We believe a rental assistance voucher could work. However, several serious problems exist with the proposal presented thus far by the Administration. If the assistance is sufficient to make the poor true consumers in the rental market, and if the volume of persons served by the program is large enough to make those eligible a force in the marketplace, I am confident that the private sector will provide efficient, quality units.

Mr. Chairman, the private market cannot support all the needed housing, especially in this time of high interest rates. Therefore, we strongly support funding for Section 8 projects that have commitments. As you know, many developers have in good faith spent considerable funds based on the Section 8 commitments they hold. However, the Administration proposes to rescind those commitments already in the pipeline for projects that are unable to receive affordable financing. We endorse Section 205 of the bill that would continue the GNMA tandem program. We note that last year the Administration did support funding of the GNMA pipeline. Such a move will increase both employment and the rental housing supply faster than any other program this Committee could support.

We applaud the introduction of your housing construction program, which is targeted to communities that are most in need. Your approach wisely avoids the multi-year commitment problem that doomed the Section 8 construction program. The targeting provision could be advantageous in constructing housing where the conventional market is unable to meet the housing demand. We offer two suggestions:

1. The subsidy required to construct and amortize the debt on rental housing is very high, especially if labor rates are excessive. Section 318 of the bill requires that Davis-Bacon rates be paid to workers on projects financed under this bill. There is no question

that Davis-Bacon forces wages up to the point that units built for the poor are sometimes the most expensive units in the area. By deleting that section of the bill, significantly more units can be built with the same dollars. At a time when there is a serious need for this housing and when unemployment is high, it is unconscionable to waste precious federal resources by requiring that already highly paid construction workers in federally assisted housing projects receive higher wages than those in non-federally assisted projects. In addition, the present apprenticeship provision discriminates against younger workers, women, and minorities. Clearly, Davis-Bacon has outlived its usefulness.

2. Section 313 defines the "Area Eligibility Criteria." The aim is to target where subsidized construction is most needed. Unfortunately, the criteria such as the "duration of rental housing vacancies" and the "extent of rental housing production lag" in many cases define the direct effect of rent control. We believe it is wrong to reward localities which, through local ordinances such as rent control, created their own rental housing problems; such communities do not deserve to be "targeted." A better use of scarce federal dollars is to help those communities trying to grapple with and realistically solve their rental housing problems.

Mr. Chairman, we would also like to say a few words about H.R. 5568, introduced by Mr. St Germain. The thrift institutions are clearly in serious trouble and the cost of saving them will be tremendous if interest rates do not moderate. Savings & Loans and Mutual Savings Banks hold over $55 billion in multifamily mortgages--Mutual Savings Banks, which are limited primarily to the Northeast, hold a greater volume of such mortgages than all the commercial banks in the country. Our Association, while taking no position on particular legislation affecting Savings & Loans, urges this body and the Administration to ease the fears held by many that a run on the thrifts could occur, leading to a collapse of confidence in all financial institutions. Whatever is done, the public must be convinced that their savings deposits are safe.

Tha caption to H.R. 5568 cites another important reason to save the thrifts--"to ensure the availability of financing for housing." Rental property is a good investment for thrifts. However, the value of any real estate security is a factor of the income the property can generate. Any local ordinance, or even the threat of one that would limit the possible earnings of a property, eliminates prudent investors. Such laws imperil the institution and increase the exposure of insurance funds which back regulated lenders. At a minimum, it causes the risk to substantially increase so lenders raise the interest rate. This increases the cost of the project, requiring the rent to also increase, making units less affordable. We want and need thrifts to invest in multifamily housing. To do so requires some assurance that their investment is safe. Therefore, we urge that an amendment be passed providing that any project financed by a loan from a federally insured institution be exempt from rent control. This proposal has the endorsement of the President's Housing Commission. Such an amendment would protect the lending institution, the federal government through its depository insurance agencies, and will lead to the construction of multifamily housing. The alternative is that non-subsidized rental housing will not be built, even when interest rates decline, in communities with rent control or the threat of rent control. Governments will then be asked to provide the needed housing supply. At a time of limited federal funds for construction, freeing private enterprise to build units would be a most cost-effective program.

This concludes my statement. Thank you for the opportunity to express the views of the National Apartment Association. I will be happy to answer any questions you may have.

Chairman **Gonzalez**. Thank you very much, Mr. Esrey. I deeply appreciate your time and patience above all, and your presentation, because you have some suggestions there and some suggested amendments that certainly will be evaluated.

In view of your time—Mr. Shiffman, do you have any objection if we proceed with the questions of Mr. Esrey and excuse him? And I will defer. I have one or two almost technical questions that I will submit with respect to the Bacon-Davis and the others.

I will defer to my colleague from New York, Mr. Rent Control, because I think he is chafing at the bit.

Mr. **Schumer**. I would just like a point of clarification before I ask a few questions. What is the National Apartment Association's view on rent control?

Mr. **Esrey**. I think it can be safely said that we are against rent control. I certainly want to get that on the record.

Mr. **Schumer**. As you know, I have been pushing for a rental production program. When I looked at the list of witnesses, I figured that the National Apartment Association, which I am not too familiar with, is going to come up here and endorse the program that we put together. But instead I find that I disagree with just about everything you said.

I see, by the way, that your remarks talked about New York and Paris. I am not familiar with the Parisienne situation. I have not been to Paris in my lifetime, but——

Chairman **Gonzalez**. You are not in the jet set?

Mr. **Schumer**. I am not in the jet set, Mr. Chairman, you know that.

But my question is: If a new apartment house is constructed in New York City, is it subject to rent control?

Mr. **Esrey**. I understand that—and I am not from New York, I am not intimately involved and I am sure that you can answer your own question better than I. But it is my understanding at one point in time that there was rent-control-free units that were supposed to be free of rent control in perpetuity, but approximately 4 years later they were brought under rent control. And I think that was the period of 1970 to 1974.

Mr. **Schumer**. I think that people in your association ought to know—and I am sure that many of them are from New York, given the large number of apartment houses we have—and the record ought to make it clear that New York City does not have rent control for newly constructed apartments. Anyone who wants to build an apartment house in New York City can build it without any rent control or rent stabilization.

Owners can opt into a rent stabilization system only if they want to, at their option, and in return the city gives them certain tax exemptions. Most of them that build—and there isn't too much being built now—enter into that system because at the bottom line they feel that rent control is less onerous than the lost burden without tax breaks.

And I dare say that a similar situation would prevail throughout the country; that if we give developers certain Federal subsidies, which I believe in doing, they would opt into a rent control system.

The other question I have has to do with abandonment. Everyone says that rent control is the major cause of housing abandonment in New York. How do you explain the housing abandonment in Philadelphia, Chicago, Cleveland, St. Louis, Baltimore, and Boston? Well, strike Boston because they now have some form of rent control, but those other cities have never had rent control at all. On the other hand they have a higher rate of housing abandonment and a lower rate of new rental construction than New York City.

On the other hand, a city like Los Angeles which has rent control has rental units being built.

Mr. ESREY. I can answer that question. I would like to go back to your first question, though, which I really did not get a chance to answer. That is, I do think that New York per se, as far as the rent control situation, always has the threat of rent control hanging over it because they have it in place.

And in fact, there was housing that was built that was free of rent control at one time, but subsequent to that, so those units came under rent control. So there is that threat.

Mr. SCHUMER. But that has nothing to do with housing abandonment.

Mr. ESREY. I was answering your previous question.

Mr. SCHUMER. Let us talk about Philadelphia or Chicago.

Mr. ESREY. I am not intimately familiar with some of those cities, but take St. Louis, which you mentioned and which I am familiar, as an example. I think that you will find two points. First, housing abandonment in those cities that you mentioned is not the degree that it is in New York, and second, that you will find that those housing units that are abandoned have become uneconomical to rehabilitate.

Whereas, in New York—and we do have clients in the New York that are fighting this problem—have housing that is very definitely economical to rehabilitate were it not for the controls that they are under.

Mr. SCHUMER. But, Mr. Esrey,—and I will allow you to submit a written answer later—I am not looking for a little bit of information about St. Louis. But if your organization is taking such a strong position against rent control, I think it is incumbent upon you to explain why there is almost no correlation between abandonment on the one hand and new construction on the other hand, in cities that have rent control and do not have rent control.

Maybe you can explain another thing to me, and that is why the most stable and, for landlords, the most profitable, parts of New York City have rent control and the most abandoned and least stable parts of New York City do not have rent control.

It is my opinion that rent control is a bugaboo. It is an easy thing for property owners to keep around and throw out and say this is the problem. It is a red flag and everyone waves it and it gets in the way of the real issues, rather than producing real results.

No property owner and no antirent control advocate has ever given me an adequate answer to that question. The one answer they all fall back on is this psychological fear that there might be rent control, and that is why rental housing is not built.

I will tell you why, in my opinion, more than anything else rental housing suffers and condominiums and things like that. It is because the tax breaks greatly favor ownership.

Mr. ESREY. There is no question.

Mr. SCHUMER. I do not see anything about that in your statement. It seems to me that if right now rentors were allowed to take deductions for interest costs and property taxes, we would find rental housing being built at the same rate, probably a greater rate than condominiums.

I have been married for a year. I rent in two places; I rent in New York and I rent here in Washington and I am getting clobbered on my taxes. And one of the things my wife and I are going to have to look for is ownership, simply because we cannot pay the taxes that we have; and our salary is way above the average person's.

It amazes me that property owners, apartment house owners, seem to ignore the tax issue which is Reaganomical and everything else, and focus on rent controls. I guess that's why rental housing gets nowhere.

Mr. ESREY. Sir, I appreciate your mentioning that because that is one of our top two priorities and has been for——

Mr. SCHUMER. What is the other one?

Mr. ESREY. Rent control is one and the tax and interest passthrough is another. We have done a great deal. We are successful in the State of Colorado in winning that victory and we do not intend to stop there. I appreciate your comments and could not agree with you more. That is one area where you and I do agree.

Mr. SCHUMER. I am glad there is one place. I can tell you, Mr. Esrey, that if the focus of our bill becomes a fight on rent control, it will do more damage to any kinds of Federal subsidy. You know, people look at your position and say, well, the owners want the Government to help them in certain ways, but when it steps in to help the tenant, that is no good.

On its face it does not make sense. Take the National Association of Realtors, for example. They are for the budget all the way except they want Government help in turning over private houses.

There has to be a modicum of fairness here. I understand that you have to represent your interest group, but I am saying that one becomes a more effective advocate when there is a little fairness.

Mr. ESREY. I think there should be a sense of fairness, and I concur that that is one thing we can do with our residents. I do want to accept your offer of submitting something for the record on rent control, because while you suggested I concentrate on St. Louis, I believe you concentrated on New York. So perhaps we can get a more varied input from around the country.

Mr. SCHUMER. For me, I can tell you that the argument that the psychological spectre of rent control deters the construction of rental housing, does not wash with me, it just does not make sense. Maybe next time you are here we can discuss Paris. I find that a little less close to home.

Mr. ESREY. I have not been there, either, but they did have similar problems, as your home city.

Mr. SCHUMER. Do they have rent control in Paris?

Mr. ESREY. Yes, they do.

Mr. SCHUMER. If I ever leave Congress, maybe I will move there. Thank you, Mr. Chairman.

Chairman **Gonzalez**. Maybe you could get on the Foreign Affairs Committee.

Mr. **Schumer**. No, I am happy here, Mr. Chairman, I am not moving. You know, New York has six people on Foreign Affairs, so we are blessed over there.

Chairman **Gonzalez**. But look how well Solarz succeeded.

Mr. **Schumer**. That is right.

Chairman **Gonzalez**. I was just going to say that you belong to the shuttle jetset right now. Also, maybe you all can get together—between New York and St. Louis, you have Chicago. Maybe that can be a middle ground. What does Chicago say about rent controls?

Mr. **Schumer**. Chicago does not have rent controls, and the statistics I have seen show that they have a higher rate of abandonment. As far as I know, Chicago never has had rent controls, except maybe during World War II. They have a higher rate of housing abandonment, a lower rate of new rental apartment house construction than New York.

Chairman **Gonzalez**. Well, thank you very much, Mr. Esrey. We really deeply appreciate your presentation and the time you have donated and your patience.

Mr. **Esrey**. Thank you, sir.

[In regard to the questions of Congressman Schumer, the following letter was received from Mr. Esrey:]

NAA
NATIONAL
APARTMENT
ASSOCIATION

SUITE 604 • 1825 K STREET, NORTHWEST • WASHINGTON, D.C. 20006 • 202/785-5111

EXECUTIVE COMMITTEE
Robert E. Esrey
President
James L. Reeder, Jr.
President-Elect
Marvin Isgur
Vice President
Roland Freeman
Treasurer
S. Cody Engle
Secretary
Gale Lively
President
Executive Officers Council
Stanley M. Taube
Chairman
National Apartment Council
Immediate Past President
Joseph C. Marcino
Chairman
National Suppliers Council
Curtis Hart
Member-At-Large
R. Alan Rudy
Member-At-Large
Raymond S. Olsen
Executive Vice President

REGIONAL VICE PRESIDENTS
William A. Bernhard, CA
Donald E. Bodley, Ph.D., KY
James T. "Jim" Chaplin, CO
Barry Gillingwater, TX
Roger Greer, GA
R.J. Kleinman, Jr., MN
Ray Maggi, CA
William G. Nash, CO
James J. Ostrowski, OH
Tex Rau, IN
Wesley Schreiber, TX
Lois I. Velasco, MN
Donald L. White, LA

COMMITTEE/BOARD CHAIRMEN
S. Cody Engle
Chairman
Bylaws Committee
Robert Sherman
Chairman
Convention Committee
Kirk Harding
Chairman
Education Committee
Foy Mickel
Chairman
Long Range Planning Committee
Barry Gillingwater
Chairman
Membership Committee
Joel Epstein
Chairman
National Apartment
Management Accreditation
Board
Ted Stellen
Chairman
National Legislative Committee
Curtis Hart
Chairman
Publications Committee

April 16, 1982

The Honorable Henry B. Gonzalez
Chairman, Subcommittee on Housing
and Community Development
U.S. House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

I would like to take this opportunity to respond to the invitation extended by Representative Charles Schumer to further comment on rent control for the hearing record of March 23, 1982.

The questions posed by Mr. Schumer addressed 1) the rate of construction and abandonment in rent controlled cities and non-rent controlled cities, 2) the reason non-rent controlled parts of New York are less profitable than those under some form of rent control, and 3) the impact of rent control on Paris.

With regard to his first question, we can find no evidence supporting the statement that the rate of new rental construction is higher in New York than in the other cities mentioned. In fact, multifamily construction in New York is almost exclusively divided between federally subsidized housing, co-operatives, and condominiums. The small amount of "unsubsidized" construction that has taken place has received significant subsidies from New York City taxpayers in the form of a generous real estate tax abatement. (Monthly Census statistics do not distinguish owner-occupied multifamily construction from rental construction. Once a year, Census does divide multifamily units by ownership status.)

As Mr. Schumer stated, those "unsubsidized" properties come under the Rent Stabilization law as a condition to receiving the tax abatements. Rent Stabilization allows these high-rent properties to charge their initial rents in an atmosphere of no controls. Therefore, if these properties are more profitable than properties in other neighborhoods--a fact we cannot document--it is due to their being exclusively high-rent properties in the initial stage of insignificant or no rent controls. The success of these new rentals in New York will depend upon the "out" years, provided they remain rentals; we suspect most will be converted to homeownership status.

Mr. Schumer contends that areas not under rent control are less profitable than those that are controlled. Those uncontrolled properties are owned by the City of New York through "in rem" tax foreclosures; New York City does not allow rent control on its

BEST DOCUMENT AVAILABLE

properties. A major reason for the non-payment of taxes, which eventually leads to titles going to the City, is the insignificant return received from the originally rent controlled buildings.

Abandonment is a fact of life in many cities. However, it is a major problem in New York with its low vacancy rate. The vacancy rate in New York is an incredibly low 2.3%. The other cities mentioned can afford to lose a portion of their housing stock, especially lower grade housing, while New York, with its infinitesimal vacancy rate, simply cannot. In fact, New York's vacancy rate has stayed low despite a greater rate of population decrease than the other cities with higher rates of abandonment. Without rent control, owners would restore and maintain their buildings. With rent control, there is no such incentive. New York's critically low vacancy rate, compared to other cities, can only be attributed to rent control.

According to a substantial study conducted by the National Urban League, lending institution disinvestment contributed heavily to the high rate of abandonment. We contend a major reason for disinvestment in New York is the lending institution's concern over rent control. George Sternlieb has pointed out that:

> "Most of the return on residential real estate comes, not from the operations of the building *per se*, but from the capacity of the owner to remortgage his building. He, thus, recaptures amortization, which frequently has severely limited his cash over a period of years . . . . The *largest single source of funds typically used by owners to rehabilitate their buildings* involved the refinancing of paid down mortgages . . . . Without financing, there can be no recovery of capital investment."
>
> (George Sternlieb, "Abandonment and Rehabilitation: What is to be Done?" A paper submitted to the Subcommittee on Housing Panels on Housing Production of the Committee on Banking and Currency, (Washington, D.C.: Government Printing Office, 1971) p. 337.)

The financial reason for disinvestment is the fear that construction or rehabilitation loans will not generate sufficient cash flow through increased rents to pay back the loan, as illustrated in certain areas of St. Louis. After a neighborhood deteriorates, it becomes impossible to attract higher rent paying tenants necessary to amortize the debt on rental property improvements. Bankers in New York tell us that they will not make loans to rent controlled properties because of the limitations, or possible limitations, on rents; rather, they concentrate their loans on 1 to 4 family unit structures that are not, and have not been, subject to rent control. In fact, data will show many New York savings banks invest a great deal of their funds in secondary market instruments despite the need for loans in New York.

Lending institutions hence are the key. Should they refuse to lend, for whatever reasons, properties will deteriorate, leading to blight and finally abandonment. Historically, lending institutions look for the smallest risk and the greatest return on their loans. Therefore, the *perceived* risks and *perceived* gain for a particular loan are important factors in abandonment.

Lenders in other cities have given us various reasons for strictly qualifying loans for apartment rehabilitation. Some of these factors could apply to New York's abandonment problem. However, while banks in other cities do not make apartment loans in *certain* areas, New York banks do not make such loans in *any* area, except in very special cases dealing with luxury buildings under modified rent control.

As you know, the Savings and Loans are in deep trouble, and Mutuals are in even deeper financial straits. We believe that an examination of the data will show that Mutuals concentrated in New York made significant rehabilitation and permanent loans on city apartments. Rent control, by limiting the return, has caused many of those loans to have outstanding balances greater than the worth of the buildings themselves. This requires the FDIC to contribute Federal dollars to the financial institutions forced to merge. Hence, we believe Federal dollars have been spent to essentially bail out the New York rent control poisoned loans. We respectfully request that this Committee have the Government Accounting Office substantiate this charge.

Paris, France is a perfect example of the problems of rent control, and what the country did to alleviate the problem. (The following statistics are taken from "France: No Vacancies" by Betrand de Jouvenel; and *Rent Control in North America and Four European Countries* by Joel F. Brenner and Herbert M. Franklin.)

First placed on properties during World War I to protect soldiers and their families, rent control laws in Paris have been modified many times. By 1929, all properties came under rent control. By 1947, a monthly rent was equivalent to the cost of half of a carton of cigarettes. Rents seldom rose above 4% of income, usually 1%. Of course, like New York, vacancies were essentially non-existent. Bribes to get vacant apartments were often over $1,500 a room. Between 1932 - 1954, almost no housing was built in or around Paris. By 1948, abandonments were running at about 10,000 buildings (not units) a year.

France wisely observed that rent control was destroying Paris. Subsequently, a slow decontrol of the older units was instituted by the government. This has allowed new units to economically compete with the controlled units, improving the housing situation in Paris. It required courageous and strong political will, but decontrol is working to save the city. Tenants may require financial assistance --but, as Paris learned, it should come from the general revenues, in the form of rental subsidies, not by rent control, which is a subsidy from a small class of apartment owners.

Today, the completely rent controlled sector is only 16% of the country's housing stock, though most of that is in Paris. This housing includes the worst housing in the country; more than 30% have no indoor toilet. The decreasing supply of rent controlled units is due to abandonments and unregulated conversions to owner-occupied units. Public housing and heavily subsidized private housing make up the majority of the housing in the city built since 1948.

I am appreciative of Mr. Schumer's invitation to provide additional comments and would request that this letter be inserted in the appropriate section of the hearing record.

Very truly yours,

Robert E. Esrey
President

Chairman **Gonzalez**. Mr. Esrey, one of the witnesses this morning suggested that the funds for the rental production program in H.R. 5731 be fair-shared rather than targeted to specific areas with severe rental housing shortages. Which do you believe is the better approach?

[At the time the hearing went to press, no comment had been received.]

Chairman **Gonzalez**. Mr. Shiffman, also, thank you.

Mr. **Shiffman**. Before Mr. Esrey leaves, in New York City, the rent controlled apartments went up in the period between 1978 to 1981 by 30 percent in terms of their rent, which is far greater than the national average. So I think you should take a look at that law.

Chairman **Gonzalez**. Thank you. Mr. Shiffman.

STATEMENT OF RON SHIFFMAN, DIRECTOR, PRATT INSTITUTE CENTER FOR COMMUNITY AND ENVIRONMENTAL DEVELOPMENT, BROOKLYN, N.Y.

Mr. **Shiffman**. Thank you very much, Mr. Chairman, and Congressman Schumer for inviting me here today to speak to you. I would like my prepared statement submitted as part of the record, as well as a supplement to it which is the study we conducted concerning the President's proposed modified section 8 program.

Chairman **Gonzalez**. Without objection, so ordered.

Mr. **Shiffman**. I will try to, because of the late hour, go through my written testimony and just touch on the highlights for you.

The Nation's housing crisis which grows more acute each day has been hidden from view by our economic problems and compounded by our country's determination at all costs to build up its military capabilities. However, the housing crisis, the overall economy and the military budget are all integrally tied together. Nowhere is this more clearly evident than in the President's 1982 and 1983 budgets.

The fiscal year 1982 low-income housing cuts and rescissions plus the proposed 1983 low-income housing cuts taken together pay for the entire proposed increase in the military budget. The issue of homes versus guns is the one that defines the parameters of our discussion today.

In New York City, the situation has reached crisis proportions. This is evident whether you analyze the latest housing surveys, ride the subways, or walk through most neighborhoods. The people who house themselves in New York's subways and in the crevices of Penn and Grand Central Stations are only the more visible of New York's 36,000 homeless individuals. They are joined by over 1.1 million renter households that had incomes below 80 percent of the area's median income, and whose chances of finding a standard affordable place to live are continually being reduced.

New York's vacancy rate in 1981 was 2.13 percent—that is a 28-percent drop in the 3 years since 1978. At the same time, contrary to those who will argue that housing quality is no longer an issue, the rate of deficiency in housing has risen by 16 percent between 1978 and 1980, and stands at more than 20 percent. The situation for our black and Hispanic neighbors in New York City is even more acute since blacks experience a housing deficiency rate of 34.5 percent and Hispanics a rate of 38.1 percent.

Parenthetically, I would like to point out that the black and Hispanic population lives in areas of New York City that have been effectively decontrolled for a great number of years.

Production programs under the President's program would be curtailed or totally eliminated in fiscal year 1983, shifting the housing burden to States, counties, and cities without the commensurate resources to accomplish the job. Housing production is not being block granted or traded in; it is being eliminated. The fact is that housing quality and availability vary from city to city, and unfortunately, national statistics tend to mask the differences among cities, often penalizing cities most in need of help.

Indeed, the Presidential Commission recognized that quality and availability problems still exist when they reported that 18.6 percent of the very low-income renters live in substandard housing. HUD, in its summary of the experimental housing allowance program results, reported that 36 percent of households with annual incomes below $8,000 live in housing that would not meet section 8 standards. Yet, the administration concluded from the EHAP study that production programs and production subsidies are not needed.

This is totally out of step with conditions in many cities, and actually contradicts the studies that were undertaken with HUD funding. Indeed, it contradicts the statement by Raymond J. Struyk, one of the scholars who reviewed the EHAP findings, that: "EHAP has contributed to evidence indicating the importance of varying the mix of housing programs in different housing markets." The administration's program to date just does not permit this kind of mix to occur.

I would like to touch on for a moment some of the proposals the President has discussed to establish a modified existing section 8 program, or what is more commonly known as the voucher program. The administration's proposal would pay the difference between 30 percent of a family's income and a reduced fair market rent. Such a program was the subject of an indepth analysis conducted by my colleague, Frank DeGiovanni, who has joined me here today.

In that study, we attempted to measure what the impact of the administration's proposal would be on New York City's population. Our major findings include identifying the need for an entitlement program, extending eligibility to include low-income families, as well as very low-income families, the maintenance of the existing fair market rent, and the need for production programs and subsidies.

I shall discuss each of these separately. First, the need for an entitlement program. I think that it is important—I do not want to go into all of the statistics, but the large number of families that are in need of the housing, in need of housing subsidies and the low turnover as well as the low number of units that the President is proposing all are indicators that if we are going to help anybody, we are really going to have to develop the voucher program as an entitlement program. The low turnover of households receiving assistance means that under currently proposed funding levels, very few additional households can be served in the future.

We believe such a program can be effective, but only if it is an entitlement program available to all those who are in need and qualify. Mind you, urging that such a program be set up as an entitlement program is nothing new. It, in essence, was an entitlement program in all the cities studied by HUD in the supply component of their EHAP experiment.

Second, the need to extend eligibility to include low-income families. In our study, we found that low-income households were as likely as very low-income households to live in substandard units and to pay excessive amounts of their income for rent. Approximately 25 percent of the low-income eligible population were living in units that did not meet quality standards, compared to 27 percent for the very low-income families.

Of the low-income households that entered the program, 68 percent did so to obtain quality housing as compared to 28 percent of the very low-income families. The basic reason for that should be pointed out—that the large majority of the recipient families, between 50 to 80 percent of the median income in New York—are actually families with children as opposed to the very low-income recipient population which are primarily elderly, single individuals.

We conclude, therefore, that restricting eligibility to very low-income families will create hardship for many households with housing problems no less serious than those the administration proposes to assist. Larger households and minority households will be particularly affected.

These groups are most likely to be represented among low-income section 8 recipients than among the very low-income section 8 recipients. Because low-income, larger families and minority residents generally lived in substandard housing when they entered the program, it is especially distressing that these households will no longer be eligible for assisted housing. We oppose the congressional limitation on eligibility to 50 percent of the median income as well as the administration's proposal to count food stamps and other noncash assistance as income.

Moreover, our proposal to use 80 percent of the median income as the standard for eligibility is consistent with those used in the study under the EHAP program.

The third point is the need for adequate payment standards. The administration's modified section 8 program would allow a household to occupy a unit renting for more than the fair market rent, with the tenant required to pay the difference between the actual rent and the fair market rent.

What we did, and I would like to point to the chart here, is we tried to see what that would mean for a family that now qualifies, and the chart that we have on the board here is typical of the average family with two children now receiving section 8 in the city of New York.

Their annual gross income is $7,764. There are four persons, two children, living in a two-bedroom apartment. The existing fair market rent in New York City for that family for two bedrooms is $407. Their monthly income is $647. After the permissible adjustments, it drops to $597.

Presently at the 25 percent level they are paying $149 and receiving a Federal rent contribution of $258. If we use the Federal proposals, the administration's proposals, then the fair market rent would drop roughly 15 percent. So the $407 fair market rent would drop to $346. And the family would see a 20-percent increase if the cap were applicable, and we are not sure the cap would be applicable for a family like this.

This means their rent after 1 year would jump to 30 percent of their adjusted income, roughly, by 20 percent of their previous rent. If the FMR is reduced by 15 percent, the second year their rent will jump to 36 percent of their income, the third year to 43 percent, and the fourth year to 52 percent.

We think this is totally untenable and it will meet the new Federal regulations. What we are basically saying is that if we follow the administration's proposal, that many of these families, given some assumptions we have made here, will in essence be in perpetuity paying 20-percent increase per month.

What we did not include here are two essential items. We did not include an increase in the base rent that may have to come in New York City because the rents may go up, and that in the future will be transferred to the tenant, and even under rent control that has been going up in New York City between 8 to 10 percent per year.

In addition to that, we did not include food stamps in the calculation, which the administration is proposing to do, and third, we did not include any passthrough for utility increases. If those are taken into consideration, the damage and the hurt to low-income families will be enormous, and we just believe that Congress must make an enormous stand on the fair market rent and the payment standards.

Finally, in terms of the voucher program we believe that the need for production programs and subsidies continues to exist. I would like to underscore the point that none of the cities examined by HUD in their EHAP study had tight housing markets. Furthermore, EHAP researchers found that cash assistance for housing does not generate major housing repairs or new construction, nor does it cause visible upgrading of neighborhoods.

Indeed, I have shown that while the administration is relying on the HUD EHAP studies to support their modified section 8 proposal, they have modified or ignored so many of the fundamental variables of that study as to render that argument untenable.

I would like Congress to review the recommendations that we made in our housing study on the vouchers because we think that it is much more in tune with the research findings of the experiment. It is inconceivable to us that at this juncture in our history, when housing opportunities for low- and moderate-income people are quickly disappearing, that our Government proposes a policy that would exacerbate rather than alleviate the problem.

We beg you to restore an element of sanity to Federal domestic policy by rejecting the administration's housing proposals, by restoring the original intent of the Brooke amendment which sets rents at 25 percent of income, including utilities, and third, by reaffirming the national commitment to producing housing for low and moderate income families by strengthening and fighting for implementaton of the Gonzalez and Schumer bills.

We welcome and applaud your efforts to develop your own legislative program. While we applaud the intent and will support the thrust of both your bills, we would like to recommend some of the following changes. First, that the level of low-income housing assistance should be increased substantially. We understand your political problem, but we think to the extent that we on the outside can help, we would like that increased.

We applaud the restitution of desperately needed funds for public housing modernization and operating subsidies and suggest more reliance in the future on the public housing concepts to provide low- and moderate-income housing.

Third, we concur with those who would like to see the section 8 new and substantial rehabilitation program replaced by a more cost-effective production program. We believe public housing to be one method. However, we do urge that funds be set aside sufficient to meet present commitments, particularly to nonprofit and community-based housing organizations so they can sustain their low income housing efforts.

In terms of the single-family homeownership stimulus and assistance program, again we generally support the extension of the 235 program. We are proud to say we have helped make that work in New York. However, we fear the 10-year term proposed may cause problems, particularly if incomes don't keep pace with inflation, and other family obligations such as the growth of the family, education and health expenses which begin to be incurred by families take place 10 years down the line.

My own son is now going to college, and 12 years after buying our home, we are less able to pay an increased mortgage than we were when we first bought our home. The concept of forebearance is good, but why have a 1.3-percent default rate to trigger it on and a half-percent to trigger it off? Why not just use the one-half percent default rate as the threshold beyond which this fund could be used.

In terms of the multi-family construction stimulus, or what we call proudly the Schumer bill, we have the following recommendations. First, the proposed amount of $1.3 billion would be consumed too quickly by new construction and therefore not produce many additional units. In order to maximize production and at the same time not penalize high cost areas with a demonstrated shortage of standard quality units, we would urge Congress to allow localities to undertake new construction only where they can demonstrate that rehabilitation is not possible or likely or economical.

Second, we believe that the 20-percent low moderate income requirement is far too low and suggest it be raised to 40 percent, with at least 25 percent being low as opposed to moderate-income families.

I would also like to propose a ceiling of 150 percent of the median to be used for determinining the eligibility of the remaining occupants.

Skipping to the fifth item in my testimony, all lower income units should be required to remain as rental units for 30 years rather than the 15 years proposed in the bill. Time passes a lot faster than we think.

Six, rents, including utilities charged to tenants, should not exceed 25 percent of their adjusted income. Seventh, while we agree with the UDAG-like criteria, we would like to make sure that high-cost cities are not penalized, and perhaps a point system that equalizes regional cost differences should be developed.

Eighth, efforts should be made to encourage the design and construction of units that will be less expensive to maintain and operate. Therefore, we would suggest that criteria that encourage long-term maintenance and operating cost reductions be developed. Included would be separate metering for utilities, cooperative sponsorship and other self-help initiatives.

Nine, due process procedures should be established, with evidentiary hearings and public hearings held prior to the approval of any rent increases. This basic tenant right should not be abrogated, and the cost accountability structure it establishes should not be avoided.

Finally, the language must be precise. "Available for occupancy" by families under 80 percent of the median income is unacceptable. Our experience with New York City's participation loan program has taught us that the legislative language must read "Occupied by" low income tenants, not just "affordable" or "available" or "within their means."

I would like to add also that we should reject any attempts by the Federal Government to restrict local efforts to regulate rents.

The Gonzalez and Schumer legislative initiatives are the only bright spot in an otherwise totally depressing housing picture. In 1974 I concluded a speech at a housing conference by saying that:

> * * * over the last 5 years, New York City has lost 36,000 housing units per year. Those cold statistics do not reflect the reality that in New York City, 100 families a day lose their homes. If a foreign enemy were to bomb five 20-family buildings a day, destroy one neighborhood every 4 months, this Nation would mobilize its resources to defeat that enemy."

Today that enemy is being aided by congressional indifference, administrative callousness and corporate greed. We urge you to rekindle congressional concern for the forgotten Americans and to assure our country's security by rebuilding our homes, preserving our neighborhoods and revitalizing our cities.

The issue is homes versus guns. The choice, however, is yours.

Thank you.

[Mr. Shiffman submitted the following material for inclusion in the record: A prepared statement; studies prepared for the Pratt Institute Center for Community and Environmental Development: "Effect of Proposed Changes in Procedures Used To Calculate Tenant Rent Contributions"; "Reasons Why Results From the Experimental Housing Allowance Program (EHAP) Should Not Be Relied Upon As Conclusive Support for the Administration's Housing Proposals"; and "Impact of a Housing Voucher Program on New York City's Population." The material follows:]

PREPARED STATEMENT OF PROFESSOR RON SHIFFMAN

The nation's housing crisis, which grows more acute each day, has been hidden from view by other economic problems and compounded by our determination to build up our military capabilities "at all costs." However, the housing crisis, the overall economy, and the military budget are all integrally tied together. Nowhere is this more clearly evident than in the President's 1982 and 1983 budgets. The Fiscal Year 1982 low-income housing cuts and recissions and the proposed 1983 low-income housing cuts taken together pay for the entire proposed increase in the military budget. The issue of "homes" vs. "guns" is the one that defines the parameters of our discussion today.

In 1981 housing starts fell to a 35-year low, dropping to below 1.1 million units. The outlook for 1982 continues to look doubtful, particularly in light of recent increases in interest rates. At the same time the National Low-Income Housing Coalition reports "a wide and growing 'housing gap' for very low-income people. . . .There are more than twice as many renter households with incomes below $3,000 as there are rental units available at 25% of their incomes. Even using a 30% rent income ratio, there is a gap of more than 1.2 million units at the very bottom of the income scale."

Unfortunately neither the administration nor congress seems willing to confront the growing threat to the security and well being of our cities and rural communities whose low-,moderate- and middle-income people are being forced to live in substandard and/or unaffordable housing units.

In New York City the situation has reached crisis proportions. This is evident whether you analyze the latest housing surveys, ride the subways, or walk through most neighborhoods. The people who house themselves in New York's subways and in the crevices of Penn and Grand Central Stations are only the more visible of New York City's 36,000 homeless individuals. They are joined by over 1.1 million renter households that had incomes below 80% of the area's median, whose chances of finding a standard affordable place to live are continually being reduced. New York's vacancy rate in 1981 is 2.13% as compared to 2.95% in 1978, which represents a loss of 17,000 available units. The vacancy rate for individuals and families at the low-, moderate- and middle-income end of the spectrum is non-existent. At the same time, contrary to those who argue that housing quality is no longer an issue, the rate of deficiency in housing has risen by sixteen per cent between 1978 and 1980 and stands at more than 22%. The situation for our Black and Hispanic neighbors is even more acute since Blacks experience a housing deficiency in 34.8% of their units and Hispanics a rate of 38.1%.

Within this context I will attempt to discuss the administration's housing proposals and their impact, particularly the "modified Section 8 existing program" proposals. I will also discuss the proposals contained in HR 5731 and HR 5750 sponsored by Congressmen Gonzalez and Schumer, respectively.

The Administration's Housing Program

The administration's housing budget and legislative program must be resoundingly rejected. Proposals to cut $23 billion from low-income housing are callous, ill-conceived, and pose an enormous threat to the viability of countless urban neighborhoods and rural communities. Indeed it should be obvious to any observer that the new initiatives being proposed and the data supporting these proposals are nothing more than a subterfuge by which the Federal government would abdicate its responsibility to provide low/moderate-income citizens with the opportunity for decent and affordable housing.

Elimination of Production Programs and Production Subsidies

The administration's proposals to rescind a substantial portion of the Fiscal Year 1982 budget would result in the loss of almost 300,000 units of new or rehabilitated housing, already approved under either the public housing or Section 8 programs. This would take place despite the critical shortage of housing that we in New York City face and despite the 20% unemployment rate in construction and allied industries. Other production programs would be curtailed or totally eliminated in Fiscal Year 1983, shifting the housing burden to states, counties, and cities without the commensurate resources to accomplish the job. Housing production is not being block granted or "traded in"— it's being eliminated.

In addition to the obvious fact that the administration would be able to transfer these savings from housing to the military budget, the proposals are based on the faulty premise that we no longer have a problem of substandard housing.

The fact is that housing quality and availability very from city to city. Unfortunately national statistics tend to mask the differences among cities, often penalizing cities most in need of help. The President's Commission on Housing reports that the proportion of dwelling units in New York City classified as deficient (19%) was more than twice the national average (7.5%). However, the Commission also noted that deficient units are prevalent in other cities. For example, more than 16% of the units in Miami and here in Washington D.C. are rated inadequate. A tragically high housing deficiency rate, coupled with the low vacancy rates cited earlier. is a dramatic indicator of the need for low- and moderate-income housing production programs. Indeed the Presidential Commission recognized that quality and availability problems exist when they reported that 18.6% of very low-income renters live in substandard housing. HUD, in its summary of the Experimental Housing Allowance Program results (EHAP - 1980 Conclusions), reported that 36% of households with annual incomes below $8,000 lived in housing that would not meet Section 8 standards. Yet, the administration concluded from the EHAP study (and others that focus on affordability issues) that production programs and production subsidies aren't needed. This is totally out of step with conditions in many cities and contradicts a statement by Raymond J. Struyk--one of the scholars who reviewed the EHAP findings -- that "EHAP has contributed to evidence indicating the importance of varying the mix of housing programs in different housing markets." The administration's program, to date, does not permit this to occur.

Proposal to Establish a Modified Existing Section 8 Program or "Voucher Program"

The administration's proposed "modified Section 8 Existing Program" would pay the difference between 30% of a family's income and a reduced fair market rent. Such a program was the subject of an in-depth analysis conducted for the Pratt Center by Frank DeGiovanni. A summary of that study is appended to this testimony. In that study we attempted to measure what the impact of the administration's proposal would be on New York City's population. Our major findings include identifying the need for an entitlement program; extending eligibility to include low-income families; and adequate payment standards. I shall discuss each of these separately.

1. Need for an Entitlement Program

The administration recognized, in part, that excessive rents are a problem for the vast majority of very low-income families, yet what they are proposing is not an entitlement program. Not only is it not an entitlement program, but it would assist only 40,000 additional families -- by a substantial reduction from the level of past years. Even at current levels, fewer households are being served than truly need assistance. In New York City, only 22%

of the 1,138,807 eligible renter households (i.e., those with incomes below 80% of the area median income) received assistance from Section 8 or public housing programs. Furthermore, the average length of residence in public housing is 11.2 years, and approximately 89% of the households that have received Section 8 since 1976 are still receiving assistance. The low turnover of households receiving assistance means that under currently proposed funding levels very few additional households can be served in the future. We believe such a program can be effective if -- but only if -- it is an entitlement program available to all those who are in need and qualify. Mind you, urging that such a program be set up as an entitlement is nothing new -- that was the nature of the programs in all the cities examined by HUD in its EHAP study.

2. Need to Extend Eligibility to Include Low-Income Families

In our study we found that low-income households were as likely as very low-income households to live in substandard units and to pay excessive amounts of their income for rent. Approximately 25% of the low-income population eligibile for Section 8 existing subsidies were living in units that did not meet quality standards, compared to 27% for very low-income families. Sixty-eight per cent of the low-income households that entered the program did so to obtain standard quality housing as compared to 28% of the very low-income families. Clearly, the severity of housing problems in New York City is not indicated solely by the size of a household's income deficiency.

We conclude therefore that restricting eligibility to very low-income families will create hardship for many low-income households with housing problems no less serious than those the administration proposes to assist. Larger households and minority households will be particularly affected.

"A comparison of the characteristics of the low-income population and the very low-income population participating in the Section 8 Existing Housing Program in New York City reveals that the two groups differ markedly. Based on past participation in the program, the households likely to be most severely affected by the change in eligibility criteria are households with children and minority households. These groups are more likely to be represented among low-income Section 8 Existing recipients than among very low-income Section 8 Existing recipients. Because low-income larger families and minority residents generally lived in substandard housing when they entered the program, it is especially distressing that these households will no longer be eligible for assisted housing."*

We oppose the congressional limitation on eligibility to 50% of the median income as well as the administration's proposal to count food stamps and other non-cash assistance as income. Instead, we recommend that eligibility to receive housing vouchers should be based on the condition of being "housing poor." We are unalterably opposed to the use of non-cash contributions and other forms of public assistance such as food stamps or school lunches as factors in calculating income. Moreover, our proposal to use 80% of the median income as the standard is consistent with that used in the EHAP study.

---

*Quotation taken from Pratt Center's Housing Voucher Study, see the attached summary, p. xii.

3. Need for Adequate Payment Standards

The administration's Modified Section 8 Program would allow a household to occupy a unit renting for more than the fair market rent with the tenant required to pay the difference between the actual rent and the fair market rent. In New York City, a reduction in the fair market rent (FMR) would exacerbate the very problem of housing affordability that vouchers were allegedly designed to alleviate. In our study we found that of the population now receiving Section 8, a 10% reduction in the payment standard would result in half of the very low-income recipients paying more than 34% of their income for rent with 25% paying more than 39% of their income for rent. The impact on current and future participants would be even more severe, since the administration proposals are likely to cut the fair market rent by about 15-20%.

We propose that the payment standards used to calculate rent subsidies remain as they are in order to allow eligible households to occupy decent housing without paying excessive proportions of income for housing costs, including utilities.

We are opposed to households being required to pay more than 25% of their income for housing including utilities. Again we are opposed to counting any non-cash contributions such as food-stamps as income for computing recipients' rent contributions. We agree with the administration's proposal to allow households to keep the difference between the payment standard and the actual rent. However, while we agree that households should be allowed to obtain units costing more than the payment if they are willing to pay the extra cash, we believe this approach can only work where there is an adequate supply of standard housing available in the area. Mind you, this is not the case in many jurisdictions where the program will be used, although it was the case in the cities in HUD's EHAP study.

4. The Need for Production Programs and Subsidies

At the outset of my testimony, I outlined our reasons for opposing the administration's proposed cutbacks in housing production programs and subsidies, which I will not reiterate. I would like to underscore the point that none of the cities examined by HUD in their EHAP study had tight housing markets. Furthermore, EHAP researchers found that "cash assistance for housing does not generate major housing repairs or new construction, nor does it cause visible upgrading of whole neighborhoods." Indeed, as I have shown, while the administration is relying on the HUD EHAP study to support their "modified Section 8" proposal, they have modified or ignored so many of the fundamental variables as to render that argument untenable. On the other hand, the recommendations put forth in the Pratt study reflect the circumstances that existed in the cities studied much more closely than do the administration's proposals.

Thus I would urge Congress to carefully review the findings and recommendations of the Pratt study. While the study is focused on New York City's experiences with the Section 8 Existing program, we believe the issues raised and recommendations made are applicable throughout the country.

It is inconceivable to us that at this juncture in our history -- when housing opportunities for low- and moderate-income people are quickly disappearing -- our government proposes a policy that would exacerbate rather than alleviate the problem. We beg you to restore an element of sanity to Federal domestic policy by:

First, rejecting all of the administration's inequitable, absurd, and heartless housing proposals, described in detail above, as well as their proposal to eliminate the rural housing program of the Farmers Home Administration and their proposals to end the Housing Counseling Programs that have helped countless families to avoid the loss of their homes;

Second, restoring the original intent of the Brooke amendment, which set rents at 25% of income including utilities;

Third, reaffirming the national commitment to producing housing for low and moderate-income families by strengthening and fighting for implementation of the Gonzalez and Schumer bills.

Comments on HR 5731 (the Gonzalez Bill) and HR 5750 (the Schumer Bill)

We welcome the House's efforts to develop a legislative program to counter the administration's disastrous housing program. While we applaud the intent and thrust of the Gonzalez bill, we would like to recommend the following changes regarding:

HUD Assisted Housing Programs

- The level of low-income housing assistance must be increased substantially. The number of units proposed still falls far short of the demonstrated need.
- We applaud the restitution of desperately needed funds for public housing modernization and operating subsidies. In addition, we strongly urge the requirement that any deficit in payments of operating subsidies to public housing authorities should be considered "rulemaking" on the HUD Secretary's part and should be subject to congressional review.

. We concur with those who would like to see the Section 8 New and Substantial Rehabilitation program replaced by a more cost-effective production program. However, we urge that funds be set aside sufficient to meet present commitments, particularly to nonprofit and community-based housing organizations so that they can sustain their low-income housing efforts.

Single Family Homeownership Stimulus and Assistance

We generally support the extension of 235 homeownership program. However, we fear that the 10-year term proposed may cause problems, particularly if incomes don't keep pace with inflation and other obligations such as family growth, education and health expenses.

The concept of forebearance is good, but why have a 1.3% default rate to trigger it "on" and ½% to trigger it "off"? Why not just use the ½% default rate as the threshold beyond which this fund could be used?

Multi-Family Construction Stimulus - The Schumer Bill

We support the intent of this bill and welcome the variety of production alternatives it makes available to substitute for Section 8 New and Substantial Rehabilitation. However, we must register the following concerns.

First, the proposed amount of $1.3 billion would be consumed too quickly by new construction and not produce many additional housing units. The numbers would depend on the depth of subsidy and could range from 60 to 100,000 units. In order to maximize production and at the same time not to penalize high cost areas with a demonstrated shortage of standard quality units, Congress should allow localities to undertake new construction only where they can demonstrate that rehabilitation isn't possible or likely.

Second, we believe that the 20% low/moderate-income requirement is far too low and suggest it be raised to 40% with at least 25% being low as opposed to moderate-income families. I would also like to propose that a ceiling of 150% of median be used for determining the eligibility of the remaining occupants.

Third, priority should be given to proposals with higher percentages of lower income families and that do not foster either long-or short-term displacement.

Fourth, we are concerned that the $13,000 - $21,660 per dwelling unit subsidy may be too shallow, particularly, since New York City's Housing Vacancy survey indicates that the Maintenance and Operating expenses as a percentage of the total rent roll has jumped from 55% in 1971 to 70% in 1981, leaving only 30% of the rent roll for debt service, vacancies and profits.

Fifth, all lower income units should be required to remain as rental units for 30 years rather than the 15 years proposed in the bill.

Sixth, rents, including utilities charged to tenants, should not exceed 25% of their adjusted income.

Seventh, the UDAG-like criteria are desirable. However, we are concerned that the criteria of per dwelling unit cost might penalize high cost cities. How will these factors be taken into account? Perhaps a point system that equalizes regional cost differences should be developed.

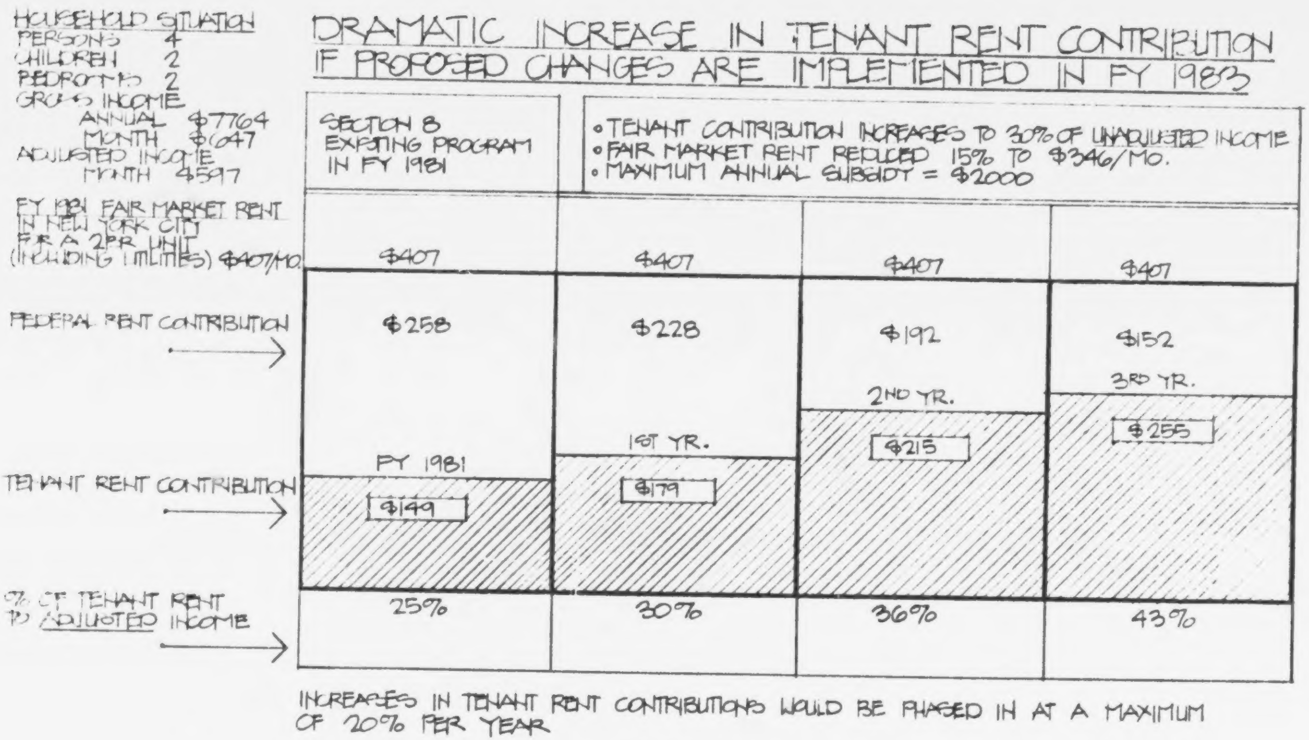
Eighth, efforts should be made to encourage the design and construction of units that will be less expensive to maintain and operate. Therefore we would suggest that criteria that encourage long-term maintenance and operating cost reduction be developed. Included would be separate metering for utilities, cooperative sponsorship,and other self help initiatives.

Ninth, "due process" procedures should be established with evidentiary hearings and public hearings held prior to the approval of any rent increases. This basic tenant right should not be abrogated and the cost accountability structure it establishes should not be avoided.

Finally, the language must be precise. "Available for occupancy" by families under 80% of median income is unacceptable. Our experience with New York City's participation loan program has taught us that the legislative language must read "occupied by" low-income tenants not just "affordable" or "available" or "within their means."

The Gonzalez and Schumer legislative initiatives are the only bright spot in an otherwise totally depressing housing picture. In 1974 I concluded a speech at a housing conference by saying that "Over the past five years New York City has lost 36,000 housing units per year. Those cold statistics do not reflect the reality that in New York City one hundred families a day lose their homes. If a foreign enemy were to bomb five twenty-family buildings a dav, destroy one neighborhood every four months, this nation would mobilize its resources to defeat that enemy." Today that enemy is being aided by congressional indifference, administrative callousness, and corporate greed. We urge you to rekindle congressional concern for the "forgotten Americans" and to assure our country's security by rebuilding our homes, preserving our neighborhoods, and revitalizing our cities. The issue is homes vs. guns -- the choice, however, is yours.

I wish to acknowledge the assistance of Brian Sullivan, Frank DeGiovanni, Rex Curry, Susan Gould, Mila Ahern and Peggy Warren in the preparation of this testimony.



DRAMATIC INCREASE IN TENANT RENT CONTRIBUTION IF PROPOSED CHANGES ARE IMPLEMENTED IN FY 1983

INCREASES IN TENANT RENT CONTRIBUTIONS WOULD BE PHASED IN AT A MAXIMUM OF 20% PER YEAR

Pratt Institute Center for Community
and Environmental Development
Pratt Architectural Collaborative

EFFECT OF PROPOSED CHANGES IN PROCEDURES USED TO CALCULATE TENANT RENT CONTRIBUTIONS

The proposed changes in procedures used to calculate the rent contributions of households participating in the Section 8 Existing Program (and in the Modified Section 8 Existing Program) will dramatically increase the proportion of the recipient's income that must be spent for rent.

The accompanying chart depicts the estimated effect of these changes on the typical (average) household with two children entering New York City's Section 8 Existing Program in 1980. At a minimum, these changes will adversely effect households coming into the program after the changes are enacted. Current Section 8 recipients will be similarly effected unless these households are permanently "grandfathered in", i.e., the proposed changes are specifically restricted to new program recipients.

The joint effect of three specific proposed changes are displayed in the chart:

. The tenant's contribution is to be increased from 25% of adjusted income to 30% of unadjusted income. (Income is currently adjusted to take into account the number of children and unusually large medical or other expenses.

. The basis for calculating the Fair Market Rent is to be changed from the median rent of all units meeting Section 8 standards, and occupied within the last two years by the current tenants, to the 40th percentile rent of all units meeting Section 8 standards, (excluding newly built units). In New York City the Fair Market Rent including utilities, for a two bedroom unit (the size needed for a household with two children) would be reduced by about 15% from $407/month, to approximately $346/month. This is an important change because the Federal rent contribution under these changes would be equal to the difference between the Fair Market Rent and 30% of the tenant's unadjusted income. If the unit's rent exceeds the Fair Market Rent, the Administration's proposals would require the tenant to pay the entire difference out of his/her pocket.*

. The average annual subsidy under the proposed Modified Section 8 Existing Program would be $2,000. The maximum annual subsidy currently is $3,600. Many households receiving Section 8 Existing assistance in New York City currently receive annual subsidies in excess of $3,000 per year.

---

* Under the current Section 8 Existing Program, tenant's are not permitted to live in units renting for more than the Fair Market Rent.

pratt 275 Washington Avenue, Brooklyn, New York 11205 Tel. (212)636-3486

The chart indicates that the typical Section 8 Existing household with two children in New York City living in a unit renting for $407/month including utilities, paid 25% of its adjusted income ($597/month) for rent, i.e., $149. Under the proposed changes, this household's rent contribution would equal 30% of its unadjusted income of $647/month - $194 - plus the entire difference between the lowered Fair Market Rent ($346) and the actual rent of the unit ($407) which amounts to $61. Thus, the tenant would have to pay $255 for rent ($194 plus $61), a sum equal to 43% of its adjusted income.

The increase in the tenants rent would not occur immediately because the program regulations impose a ceiling on the amount of rent increase a tenant can be required to pay in any one year. The current limit is a 10% annual rent increase, although the administration is proposing to raise the ceiling to 20% increase in rent per year. The chart shows how much rent the tenant would have to pay each year as the total rent increase is phased in by 20% each year. At the beginning of the third year, the tenant would be paying 43% of his/her adjusted income for rent.

This analysis is based on the assumption that these households would continue to occupy apartments renting at or near the Fair Market Rent. This is a reasonable assumption in cities like New York City that have tight housing markets (vacancy rate = 2.1%) and a substantial amount (20%) of poor quality housing. Lowering the Fair Market Rent reduces the number of standard quality units that households could rent within the Fair Market Rent level, thereby increasing the difficulty these households face in trying to find units.

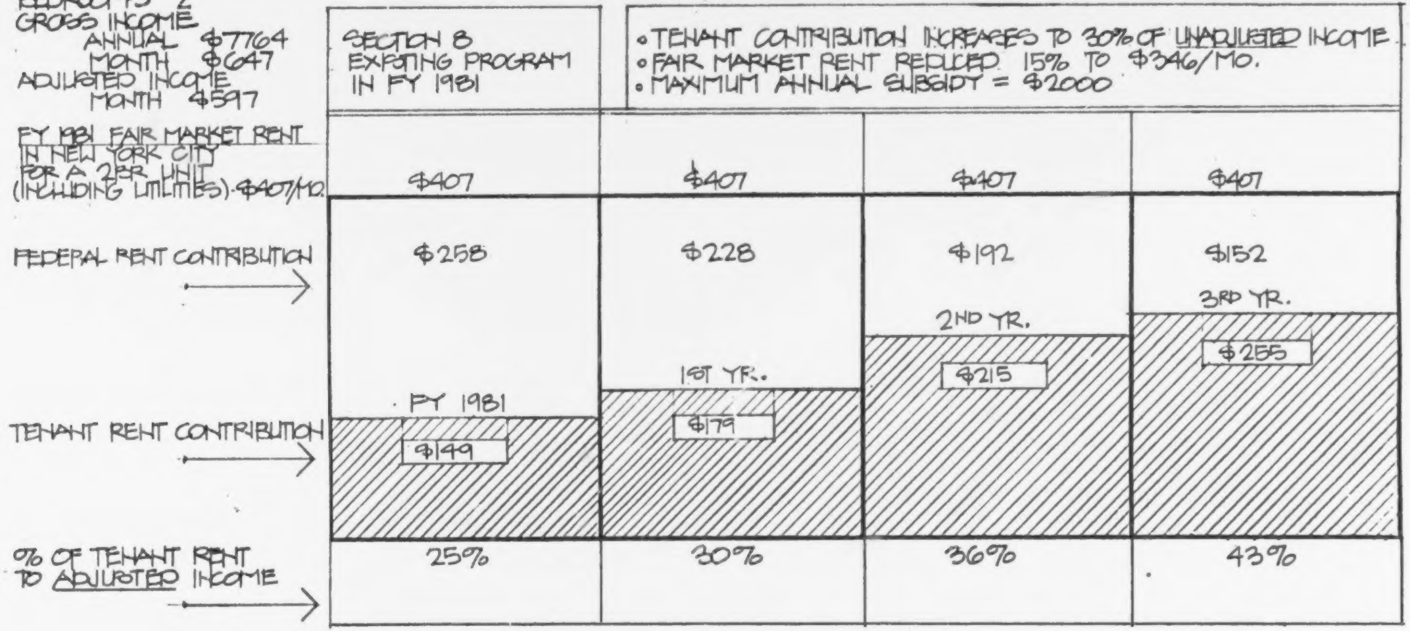
Furthermore, the estimated increase in the proportion of the tenant's income that must be spent for rent would be even greater if the likely effect of two other proposed changes are considered. First, annual adjustments in the Fair Market Rents to account for inflation and increases in landlord operating costs are proposed for elimination. If this were the case, any increase in rent levels for the five year duration of the rental assistance would have to be paid entirely by the tenant. This is likely to further increase the tenants' rent-income ratios, since it is highly doubtful that Section 8 recipients' incomes keep pace with the annual increase in rents, averaging 8.7% per year since 1978 in New York City. Secondly, the effect of including food stamps as income is not included in the chart. Such a change amounts to a 30% tax on the value of the tenants' food stamps. The combined effect of these two additional policy changes would be to dramatically increase the rent burden on these tenants even beyond the already intolerable level projected in the attached chart.

For Further Information:
(212) 636-3486
Ron Shiffman, Director
Brian Sullivan, Housing Specialist
Frank DeGiovanni, Consultant

PICCED 3/30/82

DRAMATIC INCREASE IN TENANT RENT CONTRIBUTION IF PROPOSED CHANGES ARE IMPLEMENTED IN FY 1983

HOUSEHOLD SITUATION
PERSONS 4
CHILDREN 2
BEDROOMS 2
GROSS INCOME
ANNUAL $7764
MONTH $647
ADJUSTED INCOME
MONTH $597



- TENANT CONTRIBUTION INCREASES TO 30% OF UNADJUSTED INCOME
- FAIR MARKET RENT REDUCED 15% TO $346/MO.
- MAXIMUM ANNUAL SUBSIDY = $2000

INCREASES IN TENANT RENT CONTRIBUTIONS WOULD BE PHASED IN AT A MAXIMUM OF 20% PER YEAR

Pratt Institute Center for Community
and Environmental Development
Pratt Architectural Collaborative

Pratt Institute Center for Community
and Environmental Development
Pratt Architectural Collaborative

REASONS WHY RESULTS FROM THE EXPERIMENTAL HOUSING ALLOWANCE PROGRAM (EHAP) SHOULD NOT BE RELIED UPON AS CONCLUSIVE SUPPORT FOR THE ADMINISTRATION'S HOUSING PROPOSALS

I. The Cities Studied are not Representative of Cities, Especially Large Cities in the United States

A. Population - Neither Very Large Cities Nor Rural Areas Were Studied

1. The two SMSA's studied in the supply (entitlement) demonstration ranged in size from 170,400 to 235,500.
2. The two cities studied in the demand (non-entitlement) demonstration ranged in size from 520,000 to 581,000.

B. Housing Markets - None of the Cities Had Very Tight Housing Markets

1. The vacancy rates ranged from 5.1% in Green Bay to 10.6% in South Bend, compared to 2.1% in New York City.
2. Households can be expected to experience substantially greater difficulties in trying to rely on the existing stock of housing in very tight housing markets, which commonly occur in larger cities (over 500,000).

II. Many Design Features of the Experimental Housing Allowance Program Differ from Those Recommended for the Modified Existing Section 8 Program Proposed by the Administration

A. Funding Level

1. The supply site component of EHAP was run as an open enrollment (entitlement) program available to all eligible households.
2. The administration's proposals are quite restrictive in that, very few additional households will be served by the Modified Section 8 Program.

B. Eligibility

1. EHAP based eligibility strictly on a household's inability to rent standard quality housing without paying an excessive share of its income for housing.
2. Eligibility for assisted housing programs is now being reduced to 50% of the SMSA median income by the administration, even though this does not necessarily reflect the income required to obtain standard quality housing without incurring excessive rent burdens, i.e., even families earning more than 50% of the median income may not be able to find standard quality housing without paying more than 30% of their income.

C. Rent Levels Used to Determine Household Rent Contributors

1. In EHAP a household's rent contribution was the difference between 25% of its adjusted income and the cost of obtaining standard quality housing of an appropriate size.
   - If a household found a unit renting for less than the estimated cost of standard housing, the tenant could pocket the difference.
   - If the unit rent exceeded the estimated cost of standard housing, the tenant paid the entire excess.
2. However, the Administration is proposing to change the procedures used to calculate the cost of standard housing, aka. Fair Market Rent.
   - These changes will reduce Fair Market Rent by an average of 15% to 20% in every locality.
   - Households occupying units with rents greater than this reduced Fair Market Rent will have to pay the excess themselves. In New York City, it is estimated that these changes will force renters to pay approximately 43% of their income to obtain standard quality units.

D. Results of the Experimental Housing Allowance Program (EHAP) Do Not Indicate That Housing Production Subsidies Are No Longer Needed

1. More than 25% of the rental units in the EHAP supply sites were considered substandard. Furthermore, HUD estimates that approximately 36% of households in the United States earning below $8,000 live in housing that does not meet Section 8 Existing quality standards.
2. It is widely accepted that housing allowances and the Section 8 Existing Program have not and will not increase the supply of standard housing by stimulating major rehabilitation or new construction.
3. These programs are not effective mechanisms for helping persons living in substandard units. In fact; the EHAP results indicate that households living in the worst quality housing when they enrolled in the program were the least likely to receive the rent subsidies.

For Further Information:
(212) 636-3486

Ron Shiffman, Director
Brian Sullivan, Housing Specialist
Frank DeGiovanni, Consultant

PICCED 3/30/82

COMPARISON OF MAJOR FEATURES OF THE EXPERIMENTAL HOUSING ALLOWANCE PROGRAM, THE EXISTING SECTION 8 PROGRAM, THE ADMINISTRATION'S PROPOSALS, HR 5731 AND PRATT CENTER RECOMMENDATIONS

FEATURE	EHAP	FY 1981 SECTION 8	ADMINISTRATION PROPOSALS	HR 5731	PRATT CENTER RECOMMENDATIONS
Funding Level	Entitlement in Supply Sites	90,000 total Not all are additional units	40,000 No additional units, however, all are tied to the Section 202 or the Rental Rehabilitation Program	35,000 Additional Section 8 Existing units	Entitlement or Open Enrollment
Eligibility	Income less than 4 times the cost of standard housing	80% of SMSA median income	50% of SMSA median income	80% of SMSA median income	Market basket approach. Base eligibility on households ability to rent standard units without paying excessive rent burdens
Fair Market Rent	Cost of renting standard quality housing	Median rent of all recently occupied standard units	40th percentile rent of all standard quality units, excluding new construction	No change from FY 1981 Section 8 criteria	Median rent of all recently occupied standard units
Housing Production Subsidies	None	Section 8 New, Section 8 Substantial and Moderate Rehabilitation	30,000 Units of a Rental Rehabilitation Demonstration (Authorization of $150 million)	50-100,000 Multi-family rental units ($1.3 billion authorization)	Cost-effective production programs targeted to areas with lack of standard affordable housing are needed

Pratt Institute Center for Community
and Environmental Development
Pratt Architectural Collaborative

March 29, 1982

Impact of a housing voucher program on New York City's population

By:

Frank F. De Giovanni and Mary E. Brooks

with

Ron Shiffman and Brian T. Sullivan

PREPARED
FOR THE
PRATT INSTITUTE
CENTER FOR
COMMUNITY AND
ENVIRONMENTAL
DEVELOPMENT
BROOKLYN,
NEW YORK 11205

ACKNOWLEDGMENTS

This report represents the efforts of many people. The principal researcher and technical coordinator for the project was Frank F. DeGiovanni of Pratt Institute. His scholarship, commitment, and perseverance are appreciated by all who worked with him. He was ably assisted by Mary E. Brooks, consultant to the Pratt Center, whose judgment and counsel were invaluable. Melanie Hudak and Cliff Holterman, graduate students of the Department of City and Regional Planning at Pratt's School of Architecture, assisted in the gathering of data. Brian T. Sullivan of the Pratt Center also made important contributions to the report as he has done in countless other efforts focused on providing affordable housing to low- and moderate-income persons. Assisting all of us was Peggy Krozell-Warren whose efficiency and quality of work and sense of humor kept everything moving. We also would like to thank Janet Covert for her excellent work in preparing this report for publication.

Michael Gurnee and Michael Lenauer of the Fund for the City of New York provided invaluable assistance by processing the data on invariably short notice. Detailed and insightful comments on draft revisions of the report were provided by Robert Schur, a consultant to PICCED based in New York; Bonnie Brower, Executive Director of the Association of Neighborhood Housing Developers in New York City; Cushing Dolbeare, Executive Director of the National Low Income Housing Coalition; and Kate Crawford of the National Low Income Housing Coalition. While we are grateful for their suggestions, any flaws, weaknesses, or errors in the study are, needless to say, our own.

In formulating our analysis of the Section 8 Existing Housing Program and its effects at the neighborhood level in New York City, we are indebted to the participants in the various Housing Roundtable meetings held over the past twelve months. For contributing to our understanding of the broader policy implications of the voucher proposal, we wish to thank those who gave so freely of their time and advice as part of the Transition Advisory Panel. Again, while we gratefully acknowledge the contributions of all of the above, the opinions and recommendations expressed herein in the end are truly our own.

The recommendations were developed after consultation with many individuals representing neighborhoods, private, quasi-public, and public groups; participants in the Housing Roundtable meetings; and the members of the Transition Advisory Panel. The final set of recommendations that appear in the report emerged from this process. Nevertheless, the recommendations remain those of the Pratt Center for Community and Environmental Development and are not necessarily endorsed by all the individuals who participated in the process.

And finally, for all they have done, we are grateful to Nancy Castleman of the Fund for the City of New York and Lorie Slutsky of New York Community Trust.

Ron Shiffman, Transition Project Coordinator
Director
Pratt Institute Center for Community
and Environmental Development

New York City
January 1982

PREFACE

This study was conceived by the Pratt Center for Community and Environmental Development in August, 1981 when early reports of the proposals being considered by the President's Commission on Housing and the Department of Housing and Urban Development indicated that a housing voucher program would be a centerpiece of the Commission's recommendations regarding federal programs. The purpose of the study was to determine whether the research results relied upon by the Commission in recommending a housing voucher program accurately reflected the situation in New York City. Consequently, the initial analysis focused on identifying the types of households in New York City likely to be affected by the proposals under discussion and on determining whether households issued housing vouchers in a tight housing market would experience difficulties finding acceptable housing.

The scope of the study expanded to include other issues as details of the recommendations under consideration by the Commission and the Administration emerged. Issues such as the effect of lowering the payment standard used in the Section 8 Existing Program, the possible effect of quality standards in limiting housing voucher recipients' choices of neighborhoods and the relationship between housing vouchers and neighborhood stability were examined when it became obvious that housing vouchers were being considered as a replacement for the Section 8 Existing Program and the major federal housing production subsidy programs.

Data from the 1976 Annual Housing Survey conducted in New York City, together with the results of the 1981 Housing and Vacancy Survey of New York City's rental housing market conducted by the U.S. Bureau of the Census, were relied upon to examine the nature of housing problems facing lower income households in New York City. Data describing characteristics of both recipients of Section 8 Existing rental assistance and households issued certificates but not eventually receiving the subsidy were obtained from the New York City Housing Authority. Finally interviews were conducted with representatives of neighborhood housing organizations to obtain their perceptions of the possible impacts of a housing voucher program on lower income neighborhoods.

Many of the U.S. Department of Housing and Urban Development and U.S. Office of Management and Budget preliminary proposals for a housing voucher program became public in the period between release of the draft report and this final version. The impact of some of these changes are discussed in the report. However, the specific effect of some of these changes could not be identified because the required data were not available. Moreover the final form of the Administration's proposals had not been determined as we went to press. The analysis and discussion of this report remain focused primarily on the implications of the recommendations put forward by the President's Commission on Housing in its Interim Report of October, 1981.

The findings contained in this report present a clear picture of the probable impact of various features of a housing voucher program on lower income households in New York City. These findings should be applicable, in principal, to the range of voucher programs now under consideration. Based on this analysis, a number of recommendations are made concerning the design of a housing voucher program and the need to provide some form of housing production subsidy in areas lacking an adequate supply of standard quality housing for lower income households. The Commission's Interim Report notes that production programs will still be needed in areas of inadequate supply. New York City is clearly such an area.

The findings and the recommendations endorsed in this report provide:

. concrete information which can inform the debate over the proposals for a housing voucher program;

. evidence of the impacts of many of the proposed features of a housing voucher program on housing poor households and their neighborhoods;

. a basis for neighborhood groups, coalitions, and others interested in the housing problems of lower income persons to use in seeking to affect policy decisions about assisted housing programs; and

. specific recommendations for design of a housing voucher program that we believe will best serve the needs of lower income and minority persons and their neighborhoods.

It is hoped that this report will be received and discussed by the President's Commission on Housing and its staff; others involved in housing policy within the Reagan Administration, Congress, the U.S. Department of Housing and Urban Development; public interest organizations and coalitions throughout the country; state administrations; those in New York City involved in the administration of assisted housing; and neighborhood groups and their constituencies concerned about housing in their own neighborhoods. Whatever shape the final recommendations for a housing voucher takes, we hope that the analysis and recommendations presented in this report will contribute to the development of a cost-effective housing program that will benefit the lower income population.

SUMMARY

OVERVIEW

This study was undertaken in August 1981 by the Pratt Center to identify how New York City residents would be affected by changes in assisted housing programs being considered by the President's Commission on Housing and the Reagan Administration. The findings contained in this report present a clear picture of the probable impact of various features of a housing voucher program on lower income households in New York City. Based on this analysis, recommendations are made concerning the design of a housing voucher program and the need to provide some form of housing production subsidy in areas lacking an adequate supply of standard quality housing for lower income households. Recommendations regarding the major features of a housing voucher program are presented immediately below. Recommendations specifying details of these program features are presented in the following sections of the summary.

Recommendations Regarding Major Features of a Housing Voucher Program

A housing voucher program for providing housing assistance to lower income owners and renters paying excessive proportions of their income for housing costs or those living in physically deficient housing is endorsed. However, the following guarantees must be built into such a program:

a. A housing voucher program must be an entitlement program enabling all "housing poor" to obtain standard housing.*

b. Eligibility for the housing voucher program should reflect the cost of obtaining standard quality housing and the subsistence needs of households of varying sizes in metropolitan areas. This requires a different definition of eligibility than the standard income limits currently used.

c. A housing voucher program must be accompanied by production programs where they are needed to ensure the availability of standard housing for lower income households and the preservation and maintenance of existing housing opportunities.

d. Housing units in which recipients of housing vouchers reside must be subject to reasonable, locally determined quality standards.

e. Payment standards used to calculate rent subsidies must be adequate to allow eligible households to occupy housing meeting the quality standards without paying a greater proportion of income for rent than is required by law.

---

*"Housing poor" households include renters and owners whose incomes are not adequate to obtain standard housing without paying an excessive proportion of their income for rent.

f. The subsidy under the housing voucher program should be paid directly to the recipient unless:

   1. The tenant chooses to have the payment go to the owner; or
   2. The voucher is used to secure a rehabilitation loan, in which case the payment should go directly to the owner or manager of the property.

g. Administrative funds made available to local housing authorities must be sufficient to allow a high level of support services for potential recipients and effective enforcement of housing quality standards.

h. A housing voucher program must be administered independently from all other public assistance programs, such as school lunches, food stamps, medicaid, so that payments from these programs are not included in income calculations.

i. The commitment of funds to local housing authorities for 15 years under the Section 8 Existing Program should be retained under the housing voucher program.

NEED FOR AN ENTITLEMENT PROGRAM

Findings

The President's Commission on Housing recognizes that excessive rent burdens are a problem for a majority of very low-income households, yet they state that the proposed consumer-oriented housing assistance grant should not be an entitlement program. Not only is the housing voucher program not conceived of as an entitlement program, but the number of additional units proposed for housing programs by the Reagan Administration is a substantial reduction from the levels of past years.

Few households are served by housing programs relative to the need for such assistance. This is graphically evident in New York City, where the amount of unmet need is especially large. In 1976, 1,138,802 renter households had incomes below 80% of the area median. Of these, only 22% received assistance from the Section 8 Existing Housing Program or public housing. The serious need for increased levels of housing assistance in New York City is exacerbated by the low turnover of households receiving housing assistance. The average length of residence in public housing projects in New York City is 11.2 years, and the New York City Housing Authority estimates that 89% of households that have received Section 8 rent subsidies since 1976 are still receiving assistance.

With reduced levels of program funding, the low turnover rate of program beneficiaries means that fewer additional needy households can be served in the future. Faced with such a situation, it is time to consider expanding the program to serve all those households who need assistance.

Recommendations Regarding Level of Funding

A housing voucher program for providing housing assistance to those lower income households paying excessive proportions of their income for housing costs or those living in physically deficient housing is endorsed. However, the program must be an entitlement program enabling all "housing poor" to obtain standard housing. In addition, the guarantees enumerated in the previous set of recommendations must be built into the program.

IMPACTS OF LIMITING ELIGIBILITY TO VERY LOW-INCOME HOUSEHOLDS

Findings

The Commission's analysis of national data led it to identify housing affordability as the major problem facing renters and as primarily a problem of very low-income household. Eligibility for the housing voucher program is to be restricted to very low-income households, those with incomes at or below 50% of the area median. Previously eligible low-income households (those with incomes between 50% and 80% of the area median income) would be excluded from participation.*

Limiting eligibility for assisted housing to households with incomes at or below 50% of the area median income would exclude nearly one-third of the presumably eligible renter population from participation in assisted housing programs in New York City. Similarly, 15.2% of those presently served by public housing and Section 8 Existing would no longer receive benefits if the regulations are applied to these households when their leases or contractual agreements expire.

As severe as the housing affordability problem for very low-income renters is, the restriction of program eligibility to very low-income households reflects a limited view of housing needs. An income eligibility standard set at 50% of the median income for the area may exclude many households with an affordability problem. Those "housing poor" families needing a subsidy to rent standard quality units can be more accurately identified by calculating the amount of income available for housing after the proportion of their income that must go for minimally adequate non-shelter costs is taken into account. Built into such an approach is the recognition that the proportion of income that must go for minimally adequate non-shelter consumption increases as household size increases.

Furthermore, low-income households are as likely as very low-income households to live in physically inadequate housing in New York City. Approximately 25% of the low-income population apparently eligible for the Section 8 Existing Housing Program in New York City in 1976 was living in dwelling units that did not meet quality standards, compared to 27% of the apparently eligible very low-income households.

The need of low-income households for housing subsidies to escape substandard housing is further evident if we look at the reasons indicated on New York City Housing Authority records for households entering the Section 8 Existing Housing Program. Approximately 63% of all recipients entered the program to relieve the burden of paying too much of their income for rent, while over one-third of all recipient households entering the program lived in either substandard or overcrowded units and sought relief from such housing conditions.

---

*The Housing and Community Development Act of 1981 already has imposed some limitations on the participation of low-income households in the Section 8 and public housing programs.

A large majority (68%) of the low-income households that received assistance under the Section 8 Existing Housing Program in New York City entered the program to obtain standard quality housing, compared to 28% of the very low-income recipient households. Moreover, low-income households were more than three times as likely as their very low-income counterparts to have been living in overcrowded dwelling units.

Larger households and minority households, regardless of income, appear to have a more difficult time than small households and non-minority households finding adequate accommodations which they can afford at their income level without a housing subsidy. Approximately 75% of all low-income recipient households with children entered the progam living in substandard units. They were also more likely to have been living in overcrowded dwelling units. Furthermore, approximately half of the Black, Puerto Rican, and other Hispanic households entered the program because of substandard housing, while less than 25% of white households entered the program for this reason.

These findings indicate that the incomes of many low-income households apparently are not sufficient to allow them to obtain acceptable quality accommodations without sacrificing important non-shelter subsistence needs. Clearly, the severity of housing problems in New York City is not indicated solely by the size of a household's income deficiency.

A comparison of the characteristics of the low-income population and the very low-income population participating in the Section 8 Existing Housing Program in New York City reveals that the two groups differ markedly. Based on past participation in the program, the households likely to be most severely affected by the change in eligibility criteria are households with children and minority households. These groups are more likely to be represented among low-income Section 8 Existing recipients than among very low-income Section 8 Existing recipients. Because low-income larger families and minority residents generally lived in substandard housing when they entered the program, it is especially distressing that these households will no longer be eligible for assisted housing.

Since low-income households are as likely as very-low income households to live in substandard units, and since many pay an excessive amount of their income for rent, they should not be excluded from participating in a voucher program. Restricting eligibility to very low-income households will produce hardships for many low-income households with housing problems no less serious than those faced by many of the households to be served.

Recommendations Regarding Eligibility for Housing Assistance

1. Eligibility to receive benefits from a housing voucher program should be based on the condition of being "housing poor". This requires a different definition of eligibility than the standard income limits currently used.

    a. One method of defining "housing poor" which should be considered is based on a "market basket" approach. Available shelter income is computed by identifying the total income (after taxes) by household size left after subtracting the cost of meeting basic necessities for a minimum adequate standard of living as defined by the U.S. Bureau of Labor Statistics. Any household whose available shelter income is less than the amount of money needed to obtain standard quality accommodations for a household of its size should be considered eligible for housing assistance.

b. A reduction to 50% of median area income as a basis for eligibility to receive housing assistance cannot be endorsed because it eliminates household types (including large families and minorities) that are "housing poor".

2. Unless a "market basket" approach is adopted, procedures used to compute income for eligibility determination should not be changed.

   a. Non-cash contributions from other forms of public assistance should not be included in the computation of income.

   b. Allowances for minors, higher than normal medical expenses or other unusual expenses should be retained and the allowances for minors increased.

3. Households that receive assistance under a housing voucher program should continue to receive the subsidy as long as they remain eligible for the program.

4. Administrative funds must be made available to local units of government sufficient to enable affirmative efforts to ensure that all "housing poor" households can benefit, particularly large families and minorities. Proposals to reduce the amount of administrative funds allocated to units of local government should be rejected.

PROBLEMS LIKELY TO RESULT FROM ELIMINATION OF PRODUCTION SUBSIDIES

Findings

The various voucher proposals put forward by the Administration and the President's Commission on Housing recommend termination of current housing production subsidy programs. The President's Commission, however, recognizes that some groups or areas are characterized by shortages of rental housing or a relatively large incidence of physically inadequate housing. The Commission report presents preliminary recommendations that these problems, where they exist, be addressed by other means. These include new construction as an eligible activity under tha CDBG program; providing options for State and local agency financing of housing through tax-exempt or taxable bonds; changing federal tax policy to provide a tax credit for rehabilitation or residential buildings, and encouraging private groups at the local level to sponsor and/or finance housing programs.

The supply of adequate housing for lower income persons is not likely to be increased substantially in localities if the current housing production subsidy programs are eliminated unless they are replaced with other types of subsidy programs. In this situation, households living in substandard housing at the time they are issued rent certificates or housing vouchers in tight housing markets or markets containing substantial amounts of deteriorated housing will experience great difficulty finding housing meeting program standards. The additional rent-paying ability of households with vouchers will not stimulate new construction, since, even with the subsidy, they could not afford the rent of newly constructed units.

Insight into the difficulties likely to be encountered by households issued housing vouchers in a tight housing market with a large supply of deteriorated housing was obtained by examining the experiences of households issued Section 8 certificates in New York City.

Under the able administration of the New York City Housing Authority, more than 30,000 households - 73% of those issued rent certificates - have benefited from participating in the Section 8 Existing Program since 1976, either by moving into decent quality or less crowded housing or by paying less of their own low incomes for rent. Despite this impressive accomplishment, many households issued Section 8 certificates did not receive rental assistance in New York City's tight housing market. The percentage of certificate holders that did not receive assistance appears to have increased at the same time that the vacancy rate and the length of time available units remain vacant has declined. Approximately 36% of households issued certificates after January 1, 1979 did not receive a subsidy, compared to 27% for the entire period between 1976 and 1981.

The effect of the tight housing market is further reflected in the experience of households who wanted to move or who were required to move to receive the rent subsidy. These households were substantially less likely to receive assistance than were households who were able to receive the subsidy without moving. Since the beginning of 1979, approximately 54% of certificate holders who wanted to or had to move did not receive assistance, compared to only 15% of certificate holders who were eligible to receive the assistance without moving.

The relationship between a household's wanting to or having to move to receive assistance and not receiving the subsidy is revealed very clearly in the experience of minority residents and households with children. Both in the total population of renters and among certificate holders who did obtain rental assistance, minority households and those with children were more likely than other households to occupy substandard housing. They also experienced more difficulties than other types of households using their certificates to obtain better housing. Approximately 70% of households with children and Black and Puerto Rican certificate holders wanted to or had to move to receive the subsidy, while more than 45% of certificate holders in these groups did not eventually receive the subsidy.

Although the evidence is not conclusive, it suggests that many households did not participate in the program because of the scarcity of adequate housing meeting program standards. These households would face similar, if not worse problems, finding acceptable housing under a voucher program without some effort to expand the supply of standard housing for lower income households.

Recommendations Regarding Changes in Housing Subsidy Programs

1. A housing voucher program for lower income households is endorsed only if there are sufficient production programs to ensure that standard

housing is available and maintained for "housing poor" households.

a. Those housing production programs which provide standard housing at the lowest cost primarily to the "housing poor" should be emphasized. Production programs that are shown to benefit "housing poor" households should be funded.

b. Housing production programs should be targeted to areas with a demonstrated shortage of standard housing for "housing poor" households. Examples of indicators signifying a need for production programs are a low rental vacancy rate and a short vacancy duration or the existence of a large supply of substandard housing.

c. Where adequate programs to increase the supply of standard housing for "housing poor" households in differing circumstances do not exist, they should be created. Examples of such programs are: direct production subsidies, deferred-second mortgage home purchase, improved operating subsidies for public housing, revised tax provisions to encourage maintenance of present rental housing stock, conversion of homeowner deductions to credit, subsidies for mutual housing associations or limited equity cooperatives, and additional subsidies for lower income home-ownership.

2. In addition to necessary Federal involvement, proposals to encourage private foundations, labor unions, corporations and religious institutions to provide housing and to enhance the use of pension funds for housing investment are endorsed. However, these proposals cannot be expected to have any significant effect on the production of housing units for lower income people.

3. Preservation of the existing stock of publicly assisted housing must be a priority.

EFFECT OF CHANGES IN THE PAYMENT STANDARD USED TO CALCULATE HOUSING SUBSIDIES

Findings

In its Interim Report, the President's Commission has recommended that an approach similar to that used in the Experimental Housing Allowance Program (EHAP) be adopted. A household would be free to occupy a unit renting for more than the standard used to calculate the tenant contribution, with the tenant required to pay the difference between the rent and the standard. In other words, the voucher recipient would pay more than 30% of his/her income for housing if the unit rent exceeded the payment standard. Conversely, if the recipient found a unit renting for less than the payment standard, the recipient could pocket the difference.

In New York City, even a 10% reduction in the payment standard would exacerbate the very problem--housing affordability--that housing vouchers are designed to alleviate. Dropping the payment standard 10% below the current Fair Market Rents would force a substantial number of Section 8 recipients to pay more of their income for rent if the change is applied to current program participants.

If this occurred, the 30% of the recipients living in units already renting at or above the Fair Market Rent clearly would have to pay more than 30% of their income for rent. In addition, some of the recipients whose unit rents are within 10% of the Fair Market Rents would be affected by this change. This change would fall rather hard on these households, since their rent contribution is already being increased from 25% to 30% of their income during the next five years.

Estimates of the median rent-to-income ratio likely to be paid by households receiving Section 8 assistance if the payment standard is lowered only 10% are quite dramatic. For example, half of the very low-income single elderly households would have to pay more than 34% of their income for rent; one-fourth of these same households would have to pay more than 39% of their income for rent. The impact would be equally severe for very low-income households containing one adult with children.

If the change in payment standards is not applied to current recipients, only households coming into the program after the effective date of the change would be affected. The impact on future program participants depends upon how closely the current Fair Market Rents reflect the rents actually charged in a locality for dwellings meeting program quality standards.

All available evidence suggests that lowering the payment standard would make it very difficut for households issued certificates or vouchers to locate standard quality housing renting below the payment standard in New York City's tight housing market. In such a situation, the voucher again would have failed to achieve its major purpose--alleviating the rent burdens faced by many lower income households.

Recommendations Regarding Changes in Payment Standards

1. The payment standard used to calculate rent subsidies must be adequate to allow eligible households to occupy decent housing of an appropriate size in the market area without paying excessive proportions of income for housing costs, including utilities.
   a. The median rent of all recently occupied dwelling units, including newly constructed units, should be retained as the payment standard.
   b. Any proposal to reduce the payment standard should be opposed because it will increase the difficulty of finding suitable available housing at reasonable costs.
   c. Changes in the payment standard should keep pace with changes in the cost of obtaining standard housing in each locality.
   d. The amount of funds budgeted per voucher should be adequate to ensure that households are not forced into paying excessive proportions of their income for housing costs in order to find standard housing.
2. Households should not be required to pay more than 25% of their income for housing costs, including utilities.

a. Non-cash contributions such as food stamps should not be included as income for purposes of computing program recipients' rent contributions.

b. Income allowances for minors and deductions for higher than normal medical expenses or other unusual expenses should be retained.

3. If households obtain units renting for less than the payment standard, they should be allowed to keep the difference between the payment standard and the actual rent of the unit as an incentive to keep housing costs down.

4. Households should be allowed to obtain units costing more than the payment standard if they are willing to pay the excess costs themselves.

a. However, this approach is viable only if the payment standard is reasonable and there is an adequate supply of standard housing available in the market area.

b. Any attempt to use this provision to compensate for an unreasonably low payment standard must be rejected.

THE EFFECT OF QUALITY STANDARDS ON HOUSEHOLDS AND NEIGHBORHOODS

Findings

Neighborhood groups in New York City feel that the freedom of choice provided by the Section 8 Existing Program and the proposed housing voucher program is illusory for many lower income households. Rather, they feel that the choice for many households is very limited - move or forego assistance. We have observed that households often are required to move in order to benefit from the Section 8 Existing Program. This usually occurs because their dwelling units fail to meet program standards and landlords are unwilling or unable to make the necessary repairs. This situation would also exist in a housing voucher program if standards similar to those used in the Section 8 Existing Program are adopted.

This situation poses a difficult dilemma for potential beneficiaries and creates problems for households and groups in lower income neighborhoods that are trying to upgrade the quality of neighborhood housing. If most of the available housing in these neighborhoods is of poor quality, certificate holders must choose between remaining in their neighborhood or moving to receive the rent subsidy. In addition, the application of strict quality standards may restrict the housing choices of potential recipients. And, the elimination of much of the housing in certain neighborhoods from consideration may hamper the ability of groups in these neighborhoods to improve the quality of neighborhood housing.

Neighborhood representatives interviewed indicated that many apartments that are important and unique housing opportunities for lower income families do not meet the standards currently used in the Section 8 Existing Housing Program. As was observed earlier, many of the households who must move in order to obtain the rent subsidy drop out of the program. Undoubtedly, many of these households cannot find suitable or acceptable units within the Fair Market Rents. But it is also undoubtedly true that some of these households elect not to receive benefits from the program if it means that they must leave their neighborhood or their building in order to do so.

While no one interviewed failed to recognize the importance of providing decent and suitable housing for lower income households and the contribution quality standards make toward that goal, some compromises were suggested. One suggestion offered is that in those situations where abandoned buildings are being managed by tenants or other responsible individuals or groups, households be allowed to benefit from the Section 8 Existing Housing Program or the voucher program on the condition that the apartment be brought up to program quality requirements within an agreed upon time period.

Another suggestion is that tenants be allowed to exercise flexibility in their use of Section 8 Existing certificates or housing vouchers so that they do not forfeit housing opportunities that they desire. Two examples of such circumstances are: instances where a building is converted into cocoperatives or condominiums and instances where tenants are using rents to operate the building, finance required repairs, or negotiate with the landlord for repairs.

While the administration of the current Section 8 Existing Housing standards ensures that households benefiting from the program live in good quality housing, this otherwise desirable aspect of the program may have the unintended effect of "redlining" buildings and neighborhoods. Virtual "triage" could result from households being required to move to receive the subsidy when their landlords are unwilling or unable to bring the unit up to standards, particularly in the absence of any production program.

According to interviews with neighborhood groups, such an outcome could occur for two reasons. First, the neighborhood might contain a predominance of buildings, such as old-law tenements, that are basically sound structurally but do not meet other program standards. Second, the neighborhood might contain a substantial percentage of buildings that are deteriorated. In the absence of funds to rehabilitate the properties, the households would not be able to participate in the program and remain in the neighborhood. These situations also would occur under a housing voucher program if quality standards similar to those in the Section 8 Existing Housing Program are implemented.

Neighborhood groups are concerned about the future viability of neighborhoods where much of the housing stock does not meet the Section 8 Existing quality standards. They believe that efforts should be made under the voucher program, in as many situations as possible, to enable a family to receive the subsidy in its unit if that were its choice. Furthermore, they feel that it is important to recognize that there is no evidence that the housing voucher program is being designed in such a way that the stability and cohesiveness of a neighborhood will necessarily be taken into account in the issuance of vouchers. These concerns could be addressed by permitting vouchers to be targeted, especially in conjunction with rehabilitation programs, to specific neighborhoods.

Two issues--the nature of the quality standards adopted and the ability to target vouchers to deteriorated neighborhoods by linking them with rehabilitation efforts--must be considered carefully in designing the housing voucher program. The restrictiveness of the standards becomes an even more crucial issue if the proposals to terminate present housing production programs are approved. Without production subsidies or the ability to target vouchers to neighborhoods being rehabilitated under the CDBG Program, adoption of strict standards will make it very difficult, if not impossible, for eligible households living in certain types of buildings or neighborhoods to remain in their neighborhoods and participate in the program. This, in turn, may compound the difficulties facing lower income neighborhoods as they try to improve the quality of neighborhood housing.

The efforts of neighborhood groups to improve the viability of their neighborhoods can be enhanced by providing opportunities for non-profit neighborhood based housing organizations to play an active role in the delivery of assisted housing to their neighborhoods.

Because these organizations view the provision of assisted housing as a priority concern of their constituencies, relying on neighborhood based organizations increases the likelihood of a long-range commitment to the success of a project. Such a group is likely to continue to attempt to meet the needs of its constituency to work in maintaining benefits to the neighborhood, and to emphasize the stability and future viability of the neighborhood. Assisted housing programs--including a housing voucher program--should take advantage of the skills, knowledge, and commitments that neighborhood based groups can provide in the delivery of services to their own neighborhoods.

Recommendations Regarding Quality Standards and the Role of Neighborhood Housing Groups

1. Housing units in which recipients of housing vouchers live must be subject to reasonable quality standards.

    a. Except where local standards are insufficient to define or maintain suitable housing, quality standards to ensure the health, safety and livability of housing units occupied through housing vouchers should be locally determined and administered.

    b. Federal standards must be applied where local standards are insufficient to define or maintain suitable housing.

2. Quality standards must be enforced to ensure that housing assistance recipients obtain acceptable housing and that the housing, including the provision of adequate services to occupants, is maintained at the standards. However, in cases where health and safety are not impaired, local units of government should be allowed to administer standards in association with a housing voucher program in such a way that housing choices for "housing poor" households are maximized.

    a. Examples of situations that might require flexibility in administering standards are: need for rent subsidies in neighborhoods where most of the properties do not conform to dominant standards; instances where abandoned or substandard buildings are undergoing tenant, cooperative, or other non-profit management and operation for the express purpose of bringing the building up to code; tenant-initiated or non-profit conversions to cooperatives or condominiums; and instances where tenants are using rents to operate the buildings, finance required repairs, or negotiate with the landlord for repairs.

b. Good faith efforts to meet the standards must be evident for vouchers to be used in each of these situations.

3. Persons otherwise eligible for housing assistance should not be denied assistance for any of the following reasons:

    a. The application of neighborhood quality standards, regardless of the condition of the housing unit.

    b. Discrimination from landlords on the basis of race, sex, size of household, or source of income, including the housing voucher.

    c. Private or public actions that cause housing units to become unavailable to "housing poor" households.

4. Localities should be encouraged to use all available resources, including production programs, to enable households living in substandard units to receive the voucher without being displaced.

5. The administrative funds allocated to local units of government should not be reduced, since this would threaten the locality's ability to ensure the maintenance of standards in assisted units through annual inspections.

6. Non-profit neighborhood based housing organizations should have a major role in the delivery of assisted housing to ensure that neighborhood stability is guaranteed. These roles should include: receiving contracts to publicize and market the programs; helping to define the quality standards; locating appropriate housing; and, where standard affordable housing is in short supply, developing new and rehabilitated housing.

7. Localities should be given the flexibility to target a percentage of their housing vouchers to preserve and rehabilitate the housing stock and surrounding neighborhoods, provided there are adequate guarantees against displacement.

ORGANIZATION OF THE REPORT

This report contains six chapters and an appendix. Chapter 1 presents the rationale for the report, a brief description of housing conditions in New York City and a discussion of the proposals for a housing voucher program.

Five major issues identified in response to the proposals put forth by the President's Commission on Housing, the Department of Housing and Urban Development and the Office of Management and Budget are discussed in Chapters 2 through 6. Background information, specific findings obtained in this study and summary recommendations are presented for each issue.

The need to implement housing vouchers on an entitlement basis is discussed in Chapter 2. Chapter 3 examines the impact of changes in income eligibility on lower income households in New York City. In Chapter 4, difficulties likely to be encountered by voucher recipients in the absence of housing production subsidies are discussed. The effects of lowering the payment standard used to calculate the government's share of each household's rent are identified in Chapter 5. The perceptions of representatives from neighborhood housing groups regarding the effects of housing vouchers on neighborhood stability and possible roles for neighborhood housing organizations are presented in Chapter 6.

Chapter 1

INTRODUCTION

I. WHY THIS REPORT?

In the summer of 1974, the staff of the Pratt Center began an evaluation and monitoring project that focused on the Community Development Block Grant program then still working its way through Congress. In the wake of the Nixon moratorium on housing, which had been in effect since June 1973, the program was clearly destined to shape a major part of the nation's urban policy for years to come. The Center's commitment to the equitable treatment of poor people under this program made it imperative that the Center involve itself in the public debate both nationally and in New York City. That involvement continues to this day.

Similarly, in December of 1980, Center staff predicted that the new Administration would institute sweeping changes in national policies that affect poor people. In seeking funding to begin the work necessary to deal effectively with these changes, Center staff wrote:

> The election of Ronald Reagan and the shifts of power in Congress--major in the Senate, somewhat more modest in the House--are clear indicators that there will be greater departures from existing housing and development policies than we have been accustomed to witnessing. The new initiatives and decisions to be made by the Federal government after what we expect will be a six to nine-month transition period will have a dramatic impact on New York City in general, and on the neighborhood and low-income housing movements in particular, and they will set the framework for housing and community development activity for the next decade. It is therefore imperative that we use the next few months to prepare the technical basis for the dialogue and the program development process that will inevitably follow.

Over the past six months the Reagan Administration has demonstrated an impressive level of political sophistication in obtaining quick Congressional approval for its budget and tax reduction proposals. The resultant fundamental changes in domestic policy were anticipated last December (1980), but the speed, intensity and degree of change that has taken place has surprised many knowledgeable observers.

The speed and forcefulness with which the proposal for a national housing voucher program has been brought to the fore as the centerpiece of the Administration's national housing policy is further confirmation of the ideological momentum that has built up during the first ten months of the Reagan Presidency, and the ease with which this momentum can be carried over into new program initiatives.

Therefore, it is all the more necessary that the analysis we have performed in New York City be shared with as many people as possible in order to better inform the intensifying national debate on this issue. It is in this spirit of open discussion and examination of the realities of housing the poor in the 1980s that we offer these findings for consideration and comment. It is our hope that this report will stimulate a much needed public discussion of the proposals for a housing voucher program and the eventual replacement of many housing production programs.

II. IS NEW YORK CITY TOO DIFFERENT?

One of the dangers inherent in using New York City as a vehicle for research into urban problems or programs is the time-honored cliche that New York is always the exception to every rule. And, indeed, for various purposes, New Yorkers have accepted this image and, occasionally, even promoted it when it seemed to work in their favor.

However, New York City's problems, legion as they are, may seem different from other major cities in the United States only because of their magnitude and, equally important, their timing in relation to other cities. Often, very similar problems occur in other cities on a smaller scale within a few months or years of their appearance in New York. For example, New York's fiscal "crisis" in 1975 presaged by only a short time similar crises in several Northeastern cities, some of which have not yet been as successfully resolved as has New York's (for the time being).

Comparison of data for a number of cities in the United States in 1970 and 1975 supports the view that the population of New York City is similar in many ways - proportion of minority residents, per capita and median income, age distribution - to the population of a number of other major cities.[1]

Furthermore, the renter population eligible for the Section 8 Housing Program in New York City (renter households with incomes below 80% York SMSA median family income) resembles the eligible population in three important ways. Elderly households comprise a relatively minority of eligible households in New York (31%) and throughout the U.S. (28%). Second, very low-income households represent a majority of eligible households - 68% in New York, 64% for the country proportion of the very low-income population is served by the Section 8 Program and Public Housing in New York City (22.2%) as for the U.S. as a whole (26.4%).[3]

Households receiving assistance in the Section 8 Existing Housing Program in New York City resemble in very important ways - proportion of minority recipients, proportion of recipients with very low-incomes - the characteristics of the population served by the Section 8 Existing Program nation-wide.[4] The major difference between recipients in New York City and those served nation-wide is that elderly households constitute a larger proportion of recipients in New York City than for the U.S. as a whole.

New York City does differ in some important respects from other cities, however. Residents of New York are more likely than residents of many other cities to rent their accommodations, to live inlarge multi-family structures, and to live in dense surroundings. Only Boston and Washington, D.C., of all the major cities, had comparably high proportions of renter occupied units in

---

[1] U.S. Department of Housing and Urban Development, Changing Conditions in Large Metropolitan Areas, 1980.

[2] Data describing other characteristics of the eligible renter population in New York City are not available.

[3] The data for the U.S. as a whole are obtained from Jill Khadduri and Raymond J. Struyk, Housing Vouchers: From Here to Entitlement, Urban Institute Working Paper 1536-01, December, 1980.

[4] Data describing Section 8 Existing recipients nation-wide are obtained from Abt Associates, Participation and Benefits in the Urban Section 8 Program (Cambridge, Mass.: Abt Associates, Inc., January, 1981).

1970 (the range was from 72% in Washington, D.C. to 76% in New York). Only Boston had a similar prevalence of multi-family structures (85%-88% of all residential structures). However, a number of other large cities, - Chicago, Washington, D.C., St. Louis, Cleveland, San Francisco - had concentrations of multi-family structures that were only somewhat less than that of New York City.

Finally, although the President's Commission on Housing reports that the proportion of dwelling units in New York City classified as deficient according to the Congressional Budget Office definition (nearly 19%) is more than twice the national average (7.5%), the Commission also notes that deficient units are prevalent in other large cities. More than 16% of the units in Miami and Washington D.C., for example, are rated inadequate. Although differences do exist, these comparisons indicate that, on balance, New York City is similar in many respects to other old, major cities in the U.S.

Taking a broader and more dynamic view of housing markets, New York, like many other older cities, has an extremely tight housing market (a 2.13% vacancy rate in rental units as of February/March 1981); a very active condo/coop conversion movement; pockets of gentrification in transitional residential neighborhoods; a heavy reliance on Federal funding for virtually all its initiatives in housing, but especially in new contruction and substantial rehabilitation production programs; and a population that is having a difficult time keeping up with increases in the cost of housing.

Beyond these similarities in the population eligible for housing assistance and in housing conditions, New York and other localities share one other major common characteristic--the economic context. Lower income households across the nation are suffering from the same combination of inflation, unemployment, cutbacks in public benefit programs, restrictions on entitlement grants and, perhaps most ominous of all, the clear prospect of more of the same.

Because of these reasons, the New York City experience may well be instructive in charting a course for advocates of lower income housing contesting any effort to implement a voucher program without accompanying production and rehabilitation programs. Although the effects of going to a voucher program identified in New York City may not be identical to those observed in other older, large U.S. cities with relatively tight housing markets, it is probable that a housing voucher program with the features now under active consideration by the Administration (January, 1982) will create similar patterns of effects. For example, while the same population groups excluded from participation as a result of limiting eligibility to very-low income households (those with incomes below 50% of the SMSA median income) in New York City may not be excluded in other cities, the effect of the eligibility changes is likely to fall harder on some groups than others in most cities. Which groups are most adversely affected will depend on the profile of both the previously eligible population and the households who have been most successful at participating in the Section 8 Existing Program. Similarly, the effect of a reduction in the payment standard on the rent burden of Section 8 or voucher recipients depends on the market rents in each locality.

Ultimately, officials and groups in each city will have to decide, based on their knowledge of the characteristics of the eligible population, the profile of the households receiving Section 8 Existing subsidies, and the local housing market, how applicable the findings presented in this report are to their city. Although differences may exist, we believe that reliance upon housing vouchers as the primary housing program for lower income households in other large cities with tight housing markets is likely to produce effects similar to those anticipated in New York City.

III. BACKGROUND ON HOUSING VOUCHERS

"Supply-side" subsidies have been a major component of federal housing policy since 1937 when the public housing program began. Successive federal programs have utilized land acquisition grants, interest rate reductions, tax incentives and rental subsidies, all designed to increase the availability and affordability of rental housing for lower income households.[1]

Increasingly, however, federal policymakers and especially members of Congress have been disillusioned by the steadily escalating costs of producing new and rehabilitated housing for the poor.

The dissatisfaction with the federal supply-side programs centers on three aspects of the programs. First, the per unit costs of the programs relying on new construction or substantial rehabilitation (public housing, Section 8 new construction/substantial rehabilitation, Section 236) are much higher than the per unit costs of programs, such as Section 8 Existing, which rely on the existing housing stock to meet the housing needs of lower income households. Second, the federal share of the costs of the supply programs increases sharply with increases in inflation and interest rates and the failure of tenant incomes to keep pace with increases in operating costs. Third, the federal government incurs a long term financial obligation (20-40 years) for units constructed or rehabilitated in these programs, a financial commitment both longer and larger than the 15-year obligation incurred under the Section 8 Existing Program. These concerns are expressed quite clearly in Chapter 3 of the Interim Report issued by The President's Commission on Housing.

In contrast to these supply-side interventions, the Section 8 Existing Housing Program has addressed the housing problems of lower income households with a commitment of federal funds for shorter periods of time for rent subsidies to households relying on the private sector for adequate housing.

---

[1] Throughout this paper lower income households refer generically to those households with annual incomes at or below 80% of the median income for the area - the income eligibility limit for Section 8 housing until the changes enacted in the Housing and Community Development Act of 1981 become effective.

Low-income, however, refers specifically to those households with annual incomes at or below 80% of the median income for the area but greater than 50% of the median.

Very low-income refers specifically to those households with annual incomes at or below 50% of the median income for the area.

The Section 8 Existing Housing Program has been shown to be an effective and less costly mechanism than production subsidies for reducing rent hardships experienced by lower income renters in paying for decent quality accommodations.[1] Evaluation of the Experimental Housing Allowance Program (EHAP) indicates that a housing voucher or allowance also is an effective means for making available decent quality housing affordable to lower income renters.[2]

It is not surprising, then, that the concept of housing vouchers has received such a warm welcome, at least at this stage in its definition. There is a growing consensus that something is seriously wrong with our current approach to providing housing for the poor and any radical departure from the very costly supply programs is bound to get, at least initially, a sympathetic hearing.

Although a voucher program is not a new idea, the consumer-oriented housing assistance grant program proposed by the President's Commission on Housing in its Interim Report, combined with the Commission's proposed termination of the Section 8, public housing and Section 202 programs, is a radical departure from previous federal housing policy:

> It focuses on affordability (as opposed to availability) as the major impediment to housing the nation's poor. It augments the ability of very low-income tenants to pay their rent.
>
> It requires no new mobilization of private sector resources, since existing housing (assuming it meets minimal quality standards) continues to provide shelter to rent subsidy recipients.
>
> It makes no long-term commitment of federal resources to anyone--developer, builder, owner or tenant.
>
> It proposes that only a limited number of eligible and needy households be served.
>
> It does not commit the public or private sector to add even one new dwelling unit to the nation's housing stock.[3]
>
> It imposes no national housing objectives upon localities in the distribution of their share of the federal budget devoted to rent subsidies (no site selection criteria for subsidized housing projects to worry about, etc.). Tenants find their own housing wherever the voucher enables them to afford it.

---

[1] See U.S. Department of Housing and Urban Development, Lower Income Housing Assistance (Section 8): Nationwide Evaluation of the Existing Housing Program, (Washington, D.C., 1978); and Abt Associates (1981), op.cit.

[2] See U.S. Department of Housing and Urban Development, Experimental Housing Allowance Program: Conclusions, the 1980 Report, (Washington, D.C.: The U.S. Department of Housing and Urban Development, 1980) and Raymond J. Struyk and Marc Bendick, Jr., editors, Housing Vouchers for the Poor: Lessons from a National Experiment (Washington, D.C.: The Urban Institute Press, 1981).

[3] The Commission notes that it will consider ways of dealing with supply problems in its later work. Nonetheless, the Interim Report clearly recommends termination of the Section 8, public housing and Section 202 programs.

Three major arguments in support of the approach described above are advanced by the Commission on Housing:

1. The quality of housing has improved steadily for Americans, so that today a very small proportion of households occupies substandard dwellings. The Interim Report states that a general shortage of adequate rental housing does not exist, except in some urban areas and in the rural South. Using a definition of inadequate housing developed by the Congressional Budget Office, the report estimates that approximately 7.5% of the nation's housing is in need of major rehabilitation.[1]

2. The primary housing problem of lower income households is their inability to obtain adequate accommodations without paying an excessively large proportion of their income for rent. More than 60% of very low-income renters (those with incomes less than 50% of median income) and 24% of low-income renters (those with incomes between 50% and 80% of median family income) pay more than 30% of their income for rent. Based on this and other data, the Commission concludes that affordability, rather than quality, is the primary housing problem facing the poor.

3. Experience gained through the Experimental Housing Allowance Program (EHAP) and the Section 8 Existing Housing Program has demonstrated the administrative feasibility of implementing a program that reduces rent hardship for a large number of recipients through existing housing agencies at the local level.

On the other side of the issue are not only the predictable opponents of the voucher approach, i.e., those whose financial interests are tied to the housing production industry, but also a wide range of lower income tenant advocates who see in the voucher approach not a step toward a national "entitlement" to affordable housing, but a major step backward in national housing policy as it affects the poor. Vouchers, they argue, are a prelude to the eventual withdrawal of the federal government from any commitment to lower income housing, by either supply- or demand-side intervention.

This fear has been reinforced by proposals made by OMB to rescind funds already appropriated for housing construction and rehabilitation, to demolish some existing public housing units, and to convert long term subsidy contracts to short term vouchers.[2]

---

[1] President's Commission on Housing, Interim Report, 1981, p. 15.

[2] See The Congressional Record of December 7, 1981, (Senate), pp. S14640-S14648. Earlier reinforcement of these suspicions came from an article appearing in the Washington Post of November 6, 1981, in which HUD Secretary Pierce was reported to have said that one of the advantages of replacing Section 8 with vouchers is that vouchers could be ended quickly.

Many of the objections raised against a voucher program are not directed against the concept of housing vouchers but against the way in which the voucher concept has been proposed for implementation.[1] Especially troublesome is the recommendation to eliminate current housing construction and rehabilitation programs.

Three major objections to the voucher program proposed in the Interim Report have been raised most frequently:

1. Gross aggregate figures on the national housing supply picture ignore the very real fact that housing markets are localized. Lower income tenants in many large cities have a severely restricted choice of housing opportunities available to them, even with the income supplement provided by a voucher system, because of critically low vacancy rates, especially in the non-luxury end of the rental market. Also, as the Commission notes, significant housing quality problems persist, both in major Northeastern cities and in the rural South. Replacing housing production subsidy programs with a housing voucher program will not adequately address the needs of lower income households in areas characterized by these problems.

2. One of the major justifications offered by the Commission in support of its recommendations was that a greater number of households could be served by vouchers than by supply-side programs for the same level of funding. However, recent reports of HUD and OMB Fiscal 1983 proposed budgets reveal quite clearly that the number of additional households to be served by vouchers and other subsidy programs is being reduced, not increased. The lower income restrictions for recipients (50% of median income for the SMSA) and the clearly inadequate level of funding proposed for the voucher program combine to disenfranchise millions of households who by any definition have to be counted among the "truly needy" in terms of their lack of alternatives in the present housing market. The proposed scale of operation of the voucher program is only a tiny fraction of the entitlement program envisioned by low income housing advocates.

3. Vouchers do not allow for housing to play any meaningful role in the yet to be defined national urban policy of this Administration. Besides providing shelter, federal funding for new and rehabilitated housing production programs has been the linchpin of local redevelopment and neighborhood revitalization efforts in cities throughout the country. The vouchers' single-minded focus on the affordability problem ignores the inextricable connection between investment in housing and the future viability of urban neighborhoods for their lower income residents.

---

[1] The Commission Interim Report sketched the broad features and principles of its proposed consumer-oriented housing assistance grants, leaving the detailed design work to a later report, HUD and/or Congress. Many of the details of the proposed HUD and OMB voucher programs appeared in the December 7, 1981 Congressional Record (Senate), pp. S14640-S14648.

The final details of the proposed HUD and OMB housing voucher programs are not yet known. The preliminary proposals reported in the Congressional Record, though, reveal that the basic features of the recommendations in the Interim Report appear to be reflected in the operational details of the HUD and OMB proposed programs. Although the preliminary proposals may be changed substantially before the voucher program is finally adopted, these proposals indicate the kinds of changes being considered for current housing assistance programs by the present Administration.

Fewer additional households are to be served and little help is envisioned for households in areas lacking an adequate supply of standard quality units for lower income households. Changes in the way recipient income is computed, lowered payment standards and a reduction in the maximum annual rent subsidy have been recommended. These changes would make it very difficult for program recipients in many areas to occupy standard quality units without paying an excessively high proportion of their income for rent. In addition, the proposal for a reduction in the administrative fee to be paid to Housing Authorities would jeopardize their ability to provide the services necessary to ensure the successful participation of minority households and the maintenance of buildings at the program quality standards.

This report attempts to identify the possible consequences of relying on a housing voucher program as the primary federal program addressing the housing problems of lower income households by examining the operation of the of the Section 8 Existing Housing Program in New York City.

The Section 8 Existing Housing Program is the closest programmatic approximation of housing vouchers yet implemented on a national scale. Further more, a housing voucher program of the type proposed by the President's Commission can be viewed as an extension of the Section 8 Existing Housing Program with major modifications. The potential effects of these modifications on New York City's lower income renter population are examined and recommendations regarding these changes are presented. Recommendations regarding the major features of a housing voucher program are presented in the next section of this chapter. Recommendations further specifying details of some of these program features are presented in the chapters where these program elements are discussed.

It must be emphasized that this report is not an evaluation of the New York City Housing Authority's administration of the Section 8 Existing Housing Program. Rather, the report uses the experience of this program as a means of identifying the likely impacts of a housing voucher program, implemented without accompanying rehabilitation or construction programs, on lower income renters in New York City.

IV. RECOMMENDATIONS REGARDING MAJOR FEATURES OF A HOUSING VOUCHER PROGRAM

A housing voucher program for providing housing assistance to lower income owners and renters paying excessive proportions of their income for housing costs or those living in physically deficient housing is endorsed. However, the following guarantees must be built into such a program:

a. A housing voucher program must be an entitlement program enabling all "housing poor" to obtain standard housing.[1]

b. Eligibility for the housing voucher program should reflect the cost of obtaining standard quality housing and the subsistence needs of households of varying sizes in metropolitan areas. This requires a different definition of eligibility than the standard income limits currently used.

c. A housing voucher program must be accompanied by production programs where they are needed to ensure the availability of standard housing for lower income households and the preservation and maintenance of existing housing opportunities.

d. Housing units in which recipients of housing vouchers reside must be subject to reasonable, locally determined quality standards.

e. Payment standards used to calculate rent subsidies must be adequate to allow eligible households to occupy housing meeting the quality standards without paying a greater proportion of income for rent than is required by law.

f. The subsidy under the housing voucher program should be paid directly to the recipient unless:

  i. The tenant chooses to have the payment go to the owner; or
  ii. The voucher is used to secure a rehabilitation loan, in which case the payment should go directly to the owner or manager of the property.

g. Administrative funds made available to local housing authorities must be sufficient to allow a high level of support services for potential recipients and effective enforcement of housing quality standards.

h. A housing voucher program must be administered independently from all other public assistance programs, such as: school lunches, food stamps, medicaid, so that payments from these programs are not included in income calculations.

i. The commitment of funds to local housing authorities for 15 years under the Section 8 Existing Program should be retained under the housing voucher program.

---

[1] "Housing poor" households include renters and owners whose income are not adequate to obtain standard housing without paying an excessive proportion of their income for rent.

Chapter 2

NEED FOR AN ENTITLEMENT PROGRAM

I. BACKGROUND

The President's Commission on Housing reiterates and affirms the "commitment" of the present administration to "a decent home and a suitable living environment for every American family".[1] The Commission recalls that the pursuit of this goal has traditionally involved the government in two strategies. The first is to foster conditions in the housing production and financing industries conducive to maximizing the production of housing which the majority of Americans can afford and which is suitable to their needs. The other government concern is to provide assistance to those "other" American households whose incomes are too low to enable them to participate as consumers in the market created by even a healthy private production and financing sector.[2]

The Interim Report addresses almost exclusively the second issue. It examines at length government actions designed to insure that the poor shall be adequately housed. Although the Commission recognizes that excessive rent burdens are a problem for a majority of the very low-income households, they state that the proposed consumer-oriented housing assistance grant should not be an entitlement program. And this, despite the Commission's frank recognition that even today only a small fraction of those persons whose incomes are too low to allow them to secure adequate shelter in the private housing market are being served by current public programs.

Why are officials in this country so reluctant even to espouse a true entitlement program for lower income housing? Is it because such a program would cost more than anyone might reasonably request? Yet Khadduri and Struyk estimate that an entitlement housing voucher program for households with incomes below 50% of median SMSA income would cost less than the annual allocations for current HUD programs after a phase-in period. They estimate that budget authority for an entitlement would be less than that for current programs after the third year, while outlays would be less than outlays for current programs after the sixth year of operation.[3]

It is important to realize that not only is the housing voucher program not conceived of as an entitlement program, but the number of additional units proposed by the Reagan Administration is a substantial reduction from the levels of past years. The Fiscal Year 1982 budget appropriation provides funding for 142,000 units, fewer than one-half of the units funded in 1979.

---

[1] The quoted language is from the preamble to the Federal Housing Act of 1949.

[2] The President's Commission on Housing, Interim Report, October 30, 1981, p. 1.

[3] See Khadduri and Struyk, Housing Vouchers: From Here to Entitlement, Urban Institute Working Paper 1536-01, December 1980.

Everyone is entitled to decent shelter. The Administration makes the pretense of furnishing at least minimum supplies of food, clothing, medical care and the like to all who can prove necessity. Housing programs for the poor have never been created to offer benefits to all whom the programs themselves classify as "deserving." Where the federal government endorses subsidizing households to eliminate excessive rent burdens as a means of adequately housing its poor, all those in need must be entitled to that right.

The analysis presented in this report focuses almost exclusively on lower income renters because owners are not eligible for the Section 8 Existing Program examined in this report. However, we believe that all lower income households, owners and renters, should be entitled to this assistance. Many homeowners have incomes comparable to those of renters who qualify for Section 8 assistance. In fact, analysis performed by Urban Institute staff indicates that homeowners comprise nearly 50% of all households eligible for housing allowances.[1]

The low incomes of these homeowners may prevent proper maintenance of their properties, leading eventually to deterioration of the properties. This is especially the case for low income elderly owners. Although the majority of elderly homeowners have no outstanding debt on their homes, their fixed incomes are often not large enough to afford even modest improvement costs. Participation of these and other lower income homeowners probably would help prevent further deterioration.

II. FINDINGS

The proposal for an entitlement program is based on two considerations. The first is an awareness of how few households are served by housing programs relative to the need for such assistance. This is graphically evident in New York City, where the amount of unmet need is especially large. As Table A-2 in the Appendix reveals, 1,138,802 renter households had incomes below 80% of the area median income in 1976. Of these, approximately 247,000 (22%) received assistance from the Section 8 Existing Housing Program or public housing. Approximately 216,493 owner households - 31% of all owners - also had incomes in 1976 which fell within the eligibility limit for Section 8 assistance. The nearly one million apparently eligible households not receiving a subsidy can be considered a maximum estimate of the amount of unmet need.[2]

Another, more conservative, way to estimate unmet need is to examine the proportion of presumably eligible applicants that was able to receive rental assistance. During the most recent three year period - November, 1978 - October, 1981 - 137,000 applications for the Section 8 Existing Program were received. Approximately 125,000 of these applicants were presumably eligible to participate in the program.[1] Of this number, approximately 18,000 received assistance and another 3,000 were actively searching for suitable units. Even if all 3,000 of these latter households find acceptable dwelling units, less than 17% of the presumably eligible population that sought assistance during this period was served by the Section 8 Existing Program.[2] This should be viewed as a minimum estimate of unmet need.

---

[1] Reported in Struyk and Bendick, 1981, op.cit.

[2] Even if housing assistance were offered on an entitlement basis, not all eligible households would seek to participate. The results of the EHAP open enrollment supply demonstration indicate that 42% of the eligible renters received the subsidy, although 56% of the eligible renters had enrolled in the program. Approximately 40% of all eligible homeowners enrolled in the program, although only one third of the eligible homeowners eventually received assistance. See Struyk and Bendick, 1981, op. cit.

The number of eligible households who would seek assistance under an entitlement program with active outreach efforts is likely to be greater than the number of households that have applied for the Section 8 Program. Representatives of neighborhood groups believe that, despite the long waiting list and the fact that the Section 8 Existing Program received more applications than the public housing program in 1981, many people needing housing assistance never apply for the Section 8 Existing Program. Obviously, those households that sought assistance from the Section 8 Existing Program represent only a portion of the lower income households that have a pressing housing problem.

One other piece of evidence documents the serious need for increased levels of housing assistance in New York. The turnover of households receiving housing assistance is quite small in New York City. The average length of residence in the public housing projects in New York is 11.2 years. Public housing appears to be used not as a temporary resource called upon in a time of immediate need but as a relatively permanent way to overcome the lack of resources to compete for standard quality housing on the open market. Very little turnover appears to exist among Section 8 Existing recipients also. The New York City Housing Authority estimates that approximately 89% of the households that have obtained Section 8 rent subsidies since 1976 still receive assistance.

With reduced levels of program funding, the low turnover rate of program beneficiaries means that fewer additional needy households can be served in the future. Faced with such a situation, it is time to consider expanding the program to serve all those households who need assistance.

The second consideration is that the proposal to eliminate housing production subsidies makes it even more important to implement housing vouchers on an entitlement basis. The EHAP results indicate that a housing allowance program prevents future deterioration but does not stimulate the upgrading of clearly substandard properties. At best, provision of housing vouchers to only a small fraction of eligible households would stabilize some properties but would have no impact on many other lower income properties. These properties would begin or continue to decline. At the same time, elimination of present supply-side programs and the expected reduction of funding for the CDBG program will decrease the ability of localities to rehabilitate or replace the deteriorated housing that already exists.

---

[1] These 125,000 households had incomes within the eligibility limits and were otherwise eligible according to program regulations. However, screening interviews had not yet been held with the applicants.

[2] Some of these households may have been served by public housing. However, public housing has a separate large waiting list of its own.

In this climate, provision of vouchers on an entitlement basis would stabilize a much greater proportion of the housing stock and, under the right circumstances, might induce improved maintenance of other neighborhood properties.[1]

III. RECOMMENDATIONS REGARDING LEVEL OF FUNDING

A housing voucher program for providing housing assistance to those lower income households paying excessive proportions of their income for housing costs or those living in physically deficient housing is endorsed. However, the voucher program must be an entitlement program enabling all "housing poor" to obtain suitable housing. In addition, the guarantees enumerated in the previous set of recommendations must be built into the program.

---

[1] See Struyk and Bendick, 1981, op.cit., Chapters 9 and 11 for a discussion of the possible effects of increased funding levels for housing vouchers or the Section 8 Existing Program on the neighborhood housing stock.

Chapter 3

IMPACTS OF LIMITING ELIGIBILITY TO VERY LOW-INCOME HOUSEHOLDS

I. BACKGROUND

Need to Re-examine the Definition of Housing Needs

The view that housing programs should be targeted to households with the greatest need for assistance, as recommended by the Commission, should receive universal agreement. Having agreed on this principle, however, the difficulty lies in deciding how to measure relative need for assistance.

As briefly discussed earlier, the Commission's analysis of national data led it to identify housing affordability as the major problem facing renters. Furthermore, since more than half of the very low-income households pay more than 30% of their income for rent, compared to only 22% of low-income households, the Commission concluded that "affordability is primarily a problem of the very low-income household".[1] Based on this reasoning, the Commission recommended that eligibility for the housing voucher be restricted to very low-income households, those with incomes at or below 50% of the SMSA median income.[2]

As severe as the housing affordability problem for very low-income households is, the restriction of program eligibility to very low-income households reflects a limited view of housing needs for four reasons. First, while very low- income families, as a whole, have higher rent-to-income ratios, many low-income households also pay too much of their income for rent. A housing subsidy program, therefore, which assists only very low-income households ignores what may well be equally pressing needs of households whose incomes are too high to qualify for housing assistance under the proposed eligibility limits but too low to obtain minimally acceptable housing.

Above a certain income level, however, even those who pay a very high percentage of their income for rent will have enough left over to satisfy their other wants reasonably well. These persons should not be included in a housing subsidy program. The issue lies in deciding where to draw the line. As will be argued shortly, setting eligibility for the program at 50% of SMSA median income does not necessarily restrict program benefits to those with the greatest need.

---

[1] The President's Commission on Housing, Interim Report, p.19.

[2] The change in income eligibility limits has already been enacted into law. The Housing and Community Development Act of 1981 specifies that no more than 5% of Section 8 and public housing units first made available for occupancy after the Act takes effect, and no more than 10% of the units under contract prior to the effective date of the Act and which later become vacant, can be occupied by households earning between 50% and 80% of the area median income. The Commission has recommended 50% of the SMSA median income as the eligibility limit for the housing voucher program.

Second, there clearly are other housing needs of some severity present in this country. More than five million dwelling units in the U.S. are physically inadequate[1] and approximately three million units are overcrowded.[2] Furthermore, low-income households do live in substandard dwellings. Although national statistics show that the incidence of substandard housing is greater among very low-income renters (18.6%) than among low-income renters (10.8%), the incidence of substandard conditions among low-income households may be greater in some localities than for the nation as a whole. In some areas, especially large cities with tight housing markets, low-income households may not be able to rent standard housing at all, or without paying an unreasonably high proportion of their income. Who can say that a very low-income family paying 40% of its income for rent in a standard unit is more needy than a low-income family crowded into an unsafe structure without hot water or heat because it cannot find or afford a standard unit. Without answering the unanswerable, it is safe to conclude that housing needs are not necessarily determined by relative deficiency in income alone.

Third, an adequate examination of housing needs must consider the importance of neighborhoods to individuals. In the past, housing programs often have failed to take into account the role of neighborhoods in meeting the needs of lower income households. This is reflected in the narrow focus of many housing assistance programs on the unit, ignoring the setting. When neighborhoods were considered, they often were viewed as negative influences and the neighborhoods were demolished and families uprooted.

Neighborhood conditions should be viewed as integral aspects of housing need in two ways. First, the same importance should be attached to improving neighborhood conditions as is attached to upgrading the quality of housing. This should be done sensitively, with the recognition that a neighborhood automatically should not be written off as not worth preserving for its current residents merely because it is deteriorated. Second, in recognition of the important role neighborhoods, even deteriorated neighborhoods, play in people's lives, programs, whenever possible, should be implemented in a way that promotes neighborhood stability and viability.

---

[1] The President's Commission states that 7.5% of the housing stock in 1977 was in need of major rehabilitation. This proportion increases to 13.3% for renters, 18.6% for very low-income renters and 10.8% for low-income renters. It soars to nearly 20% for Black households. President's Commission on Housing, Interim Report, 1981, Figure 2.2.

[2] According to the National Low Income Housing Coalition, the number of seriously overcrowded units (those with more than 1.5 persons per room) has increased slightly since 1976, the first increase in decades. See The National Low Income Housing Coalition, "The Low Income Housing Problem and a Proposal for Change", (Washington, D.C.: The National Low Income Housing Coalition, 1981).

To ignore the full range of circumstances that create a "housing poor" family is to continue to address only part of the problem. If we were to sum those households living in substandard quarters, those living in overcrowded units, those living in deteriorating neighborhoods, and those paying excessive amounts of their income for housing, the number of households who have severe housing needs in the country - "the housing poor" - would be several times the figure generally acknowledged by any source to date.[1]

Finally, relying on an income level for eligibility that does not adequately take into account the cost of obtaining standard quality housing and the non-shelter needs of households of varying size may exclude from participation households that have housing needs similar to those of program participants. In addition, it may not eliminate hardship for recipient households who do not have enough income left after paying rent to cover the costs of their non-shelter needs. If either of these outcomes were more than rare occurrences, it would indicate that the eligibility criterion was not adequately serving its purpose.

An income level that more accurately reflects the ability of households to afford acceptable quality units would be a better choice as the eligibility cutoff. There is an urgent need to rethink the choice of an eligibility criterion, since the Administration's recommendations to include food stamps as income and to eliminate all deductions in the computation of income also will adversely affect many lower income households with serious housing problems.

Alternative Ways to Define Housing Need

The issue of housing affordability relative to income has centered on the generally accepted standard that any household paying more than 25% of its income for housing costs is paying more than it can afford. Putting aside the question of whether the increase to 30% is more realistic for today, the use of a single percentage in examining affordability has been criticized.[2]

The standard rent-to-income ratio ignores the obvious fact that ability to pay housing costs varies with the number of persons in a household and with expenditures for non-shelter necessities.[3] Thus, affordability for housing can only be represented by a sliding scale taking into account these additonal considerations.

An example of such a calculation has been developed. The Lower Standard Budget computed by the U.S. Bureau of Labor Statistics gives the cost of basic necessities for a minimum adequate standard of living in urban areas all over the country. Identifying the income for any particular household size (after taxes) and subtracting the lower standard budget cost of meeting non-shelter needs at an adequate level provides the income left for shelter. If this residual income is less than the rent needed to acquire an acceptable quality, though non-luxury apartment, the household should be considered "housing poor" and in need of a subsidy.

---

[1] Jon Pynoos, Robert Schafer, and Chester W. Hartman, ed. Housing Urban America, updated Second Edition (New York: Aldine Publishing Company, 1980), p. 9.

[2] See Michael Stone, "Defining and Measuring Shelter Poverty" unpublished MS, (Boston: University of Massachusetts, 1981).

[3] Non-shelter necessities include food, transportation, clothing, medical care, taxes and other such costs.

For instance, in New York in 1980, according to these lower budget standards, a family of four would need an annual income of $16,682 to be able to pay for adequate non-shelter costs and pay for a unit at Fair Market Rent for the Section 8 Existing Program.[1] Four person households with incomes greater than the very low-income limit of $10,500 but less than the $16,682 needed to rent a standard unit and still meet the rest of their subsistence needs would be excluded from participation in the housing voucher program under the new eligibility standards, even if they live in substandard housing.

Similar calculations performed for the entire United States reveal that nearly 30% of all households are paying more than they can afford for housing costs.[2] Nearly 40% of all renter households and 25% of homeowner households are in this category. These total percentages are quite close to those reached using the standard 25% of income for housing costs. However, the types of households with excessive rent burdens identified by the two approaches are quite different. Rent hardships are more severe among lower income and larger households and much less severe among higher income and smaller households using the sliding standard based on differences in housing and non-shelter costs.

An approach such as this, which tries to estimate the amount of income needed to obtain decent quality housing and still meet minimum non-shelter needs, has the potential for more accurately identifying need for housing assistance. It illustrates that an income eligibility standard set at 50% of the median income for the area may exclude many households with an affordability problem. Those housing poor families needing a subsidy to rent standard quality units may be identified only by calculating the amount of income available for housing after the proportion of their income that must go for minimally adequate non-shelter costs is taken into account. Built into such an approach is the recognition that the proportion of income that must go for minimally adequate non-shelter consumption increases as household size increases.

An alternative, less precise, way to account for the greater needs of larger families would be to increase the size of the allowance for minors. Currently, households are allowed a $300 allowance for each minor. However, based on the BLS Lower Standard Budget, it appears that approximately $3000 per person is required to meet non-shelter needs. The current allowances for minors, therefore, do not seem to accurately reflect the income needs of large households.

Obviously, more analysis is needed to determine the income level which most accurately identifies need for housing assistance and to make sure that households with severe housing problems are not excluded from program eligibility by such a change. Regardless of which approach to setting eligibility is finally taken, the central point of this discussion should not be overlooked. In New York City, an eligibility level for assisted housing programs set at 50% of the SMSA median income does not accurately reflect the income required to obtain standard quality housing without incurring a rent hardship. Furthermore, it excludes households with severe housing problems from participation in the program.

---

[1] All further references to the Section 8 Program, unless otherwise noted, refer to the Section 8 Existing Program.

[2] Michael Stone, "Defining and Measuring Shelter Poverty" unpublished MS., (Boston: University of Massachusetts, 1981), p.9.

II. FINDINGS

New York City's "Housing Poor" Exhibit a Variety of Housing Needs.

Of the renter population apparently eligible for the Section 8 Existing Housing Program in New York City in 1976, nearly 27% were living in dwelling units that did not meet quality standards.[1] Another 16% were living in standard units, but paid rents above the Fair Market Rents (FMRs) established for the Section 8 Existing Housing Program. Twenty-one percent of the low-income households paid rents in excess of the FMRs. Unfortunately, data are not available to determine the proportion of all apparently eligible households paying more than 30% of their income for rent. However, the number of households with rents in excess of the Fair Market Rents provides a minimum estimate of the size of the affordability problem.[2] In addition, many households with rents below the FMRs likely paid more than 30% of their income for rent.

Contrary to the national pattern, roughly the same proportion of low-income renters and very low-income renters live in substandard units in New York City.[3] The proportions of these two groups living in substandard units are higher in New York City than for the nation as a whole. While 27% of the very low-income renters in New York City live in substandard units, 24% do so for the nation as a whole.[4] The difference is more stark for low-income households: in New York City 25% of the low-income households live in substandard units, compared to 15% for the nation as a whole. Two important conclusions emerge from these findings. First, as recognized in the Commission's report, a greater proportion of renters is living in substandard units in New York City than in the nation as a whole. Second, contrary to the U.S. as a whole, living in substandard housing is as severe a problem for low-income renter households as for very low-income renter households in New York City.

The need of low-income households for housing subsidies to escape substandard housing is further evident if we look at the reasons identified on New York City Housing Authority records for households entering the Section 8 Existing Housing Program. Most of the households who received

---

[1] These standards are developed by HUD from the Annual Housing Survey and are very similar to standards developed by the Congressional Budget Office and used by Abt Associates to estimate the adequacy of housing among households eligible for the Section 8 Existing Housing and New Construction Programs. See Abt Associates, Participation and Benefits in the Urban Section 8 Program (Cambridge, Mass: Abt Associates, Inc., January, 1981)

[2] Households with incomes very close to the upper limit for program eligibility (80% of SMSA median) are possible exceptions.

[3] Very low-income households comprise nearly two-thirds of the eligible population in New York City, with the remaining one-third consisting of low-income households.

[4] Data for the U.S. as a whole are reported in Khadduri and Struyk, 1980, op.cit. The incidence of substandard housing among low-income renters cited in the Commission's Interim Report (10.8%) is smaller than the figure cited by Khadduri and Struyk. The discrepancy may be due to the use of different quality standards.

Table 1

Reason Given for Households' Entering the Section 8 Existing Program in New York City[a]

Recipient Category	Substandard Housing	Rent Hardship	Other	Total
	Reason Given			
Household Type				
Single Non-Elderly	35.4%	62.1%	2.5%	100.0%
Single Elderly	21.9	74.3	3.7	100.0
One Adult w/Children	51.9	46.7	1.4	100.0
Two Adults w/Children	55.1	41.9	3.0	100.0
Two Elderly	23.6	72.2	4.2	100.0
Two Non-Elderly	37.8	59.5	2.7	100.0
Income				
Low-Income	67.5	29.8	2.7	100.0
Very Low-Income	27.6	69.3	3.1	100.0
Race/Ethnic Group				
White	20.0	76.9	3.1	100.0
Black	49.6	47.7	2.7	100.0
Puerto Rican and Other Hispanic	50.2	44.3	5.5	100.0
Other	35.3	61.6	3.1	100.0
Number of Bedrooms Required				
0	14.6	81.9	3.5	100.0
1	27.3	69.3	3.4	100.0
2	50.6	46.9	2.5	100.0
3	59.0	39.5	1.5	100.0
4	61.5	37.3	1.2	100.0
Total	33.9	63.0	3.1	100.0

[a] The reason for entry into the program is identified by the Housing Authority staff at the time of application to the program.

Source: New York City Housing Authority Records

assistance entered the program to reduce the proportion of their income that they spent for rent.[1] Prior to entering the program these households generally devoted more than 40% of their income to housing. While the majority - 63% - of all recipients entered the program to relieve the burden of paying too much of their income for rent, over one-third of all households sought assistance because they lived in either substandard or overcrowded housing conditions. (See Table 1).

A large majority (68%) of the low-income households that received assistance under the Section 8 Existing Housing Program in New York City entered the program to obtain standard quality housing, compared to 28% of very low-income recipient households.[2] Moreover, low-income households are more than three times as likely as their very low-income counterparts to have been living in overcrowded dwelling units.

Some household types are more likely than others to enter the program to obtain better housing. Larger households and minority households, regardless of income, appear to have a more difficult time than small households and non-minority households finding adequate accommodations which they can afford at their income level without a rent subsidy. Approximately 75% of all low-income recipient households with children (thus, the larger households) entered the program living in substandard units.[3] These larger households also were more likely to be living in overcrowded dwelling units. Furthermore, approximately half of the Black, Puerto Rican and other Hispanic households entered the program because of substandard housing, while less than 25% of white households entered the program for this reason.

This difference is even greater when households are compared by race within each of the two income groups. Over 70% of low-income Black, Puerto Rican and other Hispanic households indicated substandard housing as their reason for entering the program, compared to 54% of the white households. At the same time, less than 22% of very low-income white households indicated they entered the program because they were living in poor quality housing, compared to 50% for Puerto Ricans, 42% for Blacks and 35% for other Hispanics.

---

[1] The Housing Authority staff identified whether households with eligible incomes qualified for assistance because they lived in substandard housing, had excessively high rent-income ratios (usually greater than 40%), had been displaced, etc. Most of the households identified as entering the program because of rent hardship did not also live in substandard housing, since 89% of these households were able to receive the subsidy without moving (this assumes that households who received assistance in place did so because their units were of acceptable quality, not because their landlords repaired previously substandard units).

[2] Part of the reason for this difference is that New York City requires that households that want to enter the program to reduce their rent-income ratio in their dwelling unit be paying 40% or more of their income for rent. Because low-income households are less likely than very low-income households to pay such an excessive amount of their income for rent, they are less likely to enter the program on this basis. The fact that low-income households are less apt to qualify for the program because of rent hardship does not alter the conclusion that low-income households benefit from the program in terms of improved housing conditions and it does not alter the conclusion that these needs exist.

[3] Approximately 53% of all recipient households with children entered the program to improve their housing conditions.

Although the number of low-income households seeking Section 8 benefits because of rent hardship is overshadowed by those seeing to move from substandard units, we should not lose sight of the fact that many (30%) of the low-income recipients had severe rent burdens (rents in excess of 40% of their income) when they sought assistance.

These findings indicate that the incomes of many low-income households in New York City apparently are not sufficient to allow them to obtain acceptable quality accommodations without sacrificing important non-shelter subsistence needs. Clearly, the severity of housing problems in New York City is not indicated solely by the size of a household's income deficiency.

As a consequence, an eligibility cutoff pegged at 50% of the SMSA median income excludes from program benefits many households with serious housing problems. Performing a similar analysis using an alternative standard based on the "market basket" approach discussed earlier would reveal whether the alternative standard would more accurately identify households who cannot afford to rent units meeting program standards without incurring a severe rent hardship. Unfortunately, we are unable to perform such an analysis.

The Effects of Changes in Eligibility Will Fall Unevenly on Certain Types of Households

The characteristics of the low-income population indicate that a housing voucher program that limits eligibility to very low-income households will affect certain sectors of the eligible population more severely than others.

Recommendations to limit eligibility for assisted housing to households with incomes below 50% of the median income for the area would exclude nearly one-third (32.3% or 267,761 households) of the presumably eligible renter population from participation in housing programs in New York City.[1] Similarly, 15.2% of those presently served by public housing and Section 8 Existing (30,188 households) would no longer be able to receive benefits if the regulations are applied to these households when their leases or contractual agreements expire.

Of all currently eligible renter households in New York City, those comprised of two adults with children and of two non-elderly persons have the highest proportion (46%) with low incomes as opposed to very low incomes. These household types will be hurt disproportionately more than other households by the change in income eligibility requirements.

Additional data describing the characteristics of the low-income population are not available. However, we can learn more about the households that are likely to be hurt by the change in income eligibility by identifying the composition of low-income households receiving Section 8 Existing assistance. Because these households applied for the Section 8 Program, they are self-selected and may not be representative of the low-income population as a whole. However, since these households did seek assistance from the Section 8 Program, it is reasonable to assume that they are representative of the low-income households who likely would participate in a housing voucher program if the income limit for eligibility is not changed. As a result, they are the households likely to be most adversely affected by the change in eligibility.

---

[1] These households appear eligible on the basis of their income. Some unknown proportion of these households probably would be found ineligible by the Section 8 Program screening interview.

Before we proceed with this analysis, however, it is important to develop an overview of the types of New York households served by the public housing and Section 8 Existing programs in order to understand how the needs of different types of households are being served by the programs.

A vast majority (84%) of the households living in public housing and receiving Section 8 Existing assistance in New York City are classified as very low-income households. For the nation as a whole, this figure is 80%.[1]

Very low-income households are also served by welfare assistance. More than 340,000 households receive welfare shelter allowances in New York City. Despite this shelter allowance, these households typically occupy some of the worst housing in the City. Although discrimination undoubtedly explains some of this, the most important reason is that the welfare shelter allowance is not large enough for households to rent acceptable quality units. As of October 1981, the Fair Market Rents (FMRs) for the Section 8 Program were slightly more than double the shelter allowances. The shelter allowances in New York City have not been increased since 1975. At the same time, the quality of lower cost rental housing has declined as maintenance and operating costs have risen faster than the rent-paying abilities of poorer tenants.[2]

Although the public housing and Section 8 Existing Programs are each targeted to very low-income households, the populations served by these two programs are quite different. Nearly 85% of the 171,585 households living in public housing are minority residents. More than half of these households contain 3 or more persons. Approximately 33% of the households living in public housing are comprised of one adult and children, while only 27% of the households are headed by an elderly adult (age 62 years or older).

The population served by the Section 8 Existing Program, on the other hand, is older and comprised of fewer minority households. More than 53% of the 30,188 households receiving a subsidy from the Section 8 Existing Program are elderly households, while less than 25% of the households contain 3 or more persons. Approximately 48% of the households residing in Section 8 assisted units are minority households, with the minority households substantially more likely than white households to contain children (49% versus 14% percent).

When all publicly assisted housing programs are examined, it is clear that the needs of most, if not all, types of households are being addressed by the total array of programs.[1] However, it appears that the housing problems of different groups are addressed primarily by different programs.[2] For example, the large percentage of elderly among the Section 8 Existing recipients reflects the City's decision to allocate a major share of its Section 8 Existing certificates to elderly households. Approximately 63% of the Section 8 Existing certificates available for the years 1979-1982 were allocated to elderly households in the City's Housing Assistance Plan (HAP) submitted as part of its Seventh Year Community Development Application.

---

[1] The data for the U.S. were obtained from Khadduri and Struyk, 1980, op.cit.

[2] For a discussion of this problem, see Bruce Gould, An Examination of the Current Maximum Rent Levels in New York City, New York City Department of Housing Preservation and Development, July 1981.

A comparison of the characteristics of the low-income population and the very low-income population participating in the Section 8 Existing Program in New York City reveals that the two groups differ markedly.[3] The low-income recipient households have the following characteristics:

> A large proportion are minority (65.8% are Black, and 15.2% are Puerto Rican and other Hispanic);
>
> A majority are households with children (51.7% of the households contain one parent with children and 24.6% of the households have two parents with children), while only 17% are elderly;
>
> Approximately 19% need apartments with at least three bedrooms, while only 23.6% need apartments with one or less bedrooms;
>
> A large proportion (72%) wanted to or were required to move to receive benefits from the Section 8 Existing Program. (This is true even when controlling for the number of bedrooms, for racial and ethnic group, and for household type); and
>
> A large proportion of elderly households are white.

In contrast, the very low-income recipient households have the following characteristics:

> A majority (58.3%) are white:[4]
>
> A majority are elderly households (60.3%), while only 22.1% had children in the household;
>
> A large proportion need apartments with one or less bedroom (67.6%);
>
> A small proportion wanted to or were required to move to receive benefits from the Section 8 Existing Program (35.6%); and
>
> Only single non-elderly and one adult with children households are predominantly minority (the latter is 82.0%).

---

[1] As is true for the U.S as a whole, a relatively small proportion of the overall need is served by all programs.

[2] Proposals to drastically reduce the funding for new public housing units and to emphasize reliance on the existing housing stock would most adversely affect those households in New York City - minorities, large families - whose needs are met primarily by the public housing program.

[3] Comparable data describing the characteristics of low-income and very low-income public housing residents are not available.

[4] This reflects the City's decision to allocate the majority of Section 8 certificates to elderly applicants, most of whom are white.

The households most severely affected by the change in eligibility criteria are households with children and minority households.[1] These groups are not represented in large numbers among the very low-income Section 8 Existing recipients. It is especially distressing that low-income larger families and minority residents will no longer be eligible since these households generally lived in substandard housing when they entered the program.[2]

Since low-income households are as likely as very-low income households to live in substandard units, and since many pay an excessive amount of their income for rent, they should not be excluded from participating in the voucher (or Section 8) program. Restricting eligibility to very low-income renters will produce hardships for many low-income households with housing problems no less serious than those faced by many of the very low-income households served.

A more pragmatic, though no less important, consideration is that reducing the eligibility limit threatens the viability of many local rehabilitation programs. Community Development funds often finance the rehabilitation of buildings that are still occupied. Low-income residents of these buildings cannot pay the restructured rents without allocating an excessive proportion of their income for rent unless they receive a rent subsidy from the Section 8 Existing Program. Eliminating these households from Section 8 or voucher eligibility either will prevent the building from being renovated or will create a rent hardship for the low-income residents living there. Such a situation would be inequitable, as households with incomes just above the eligibility cutoff will pay a greater percentage of their income for rent than will households with incomes just under the eligibility cutoff.

III. RECOMMENDATIONS REGARDING ELIGIBILITY FOR HOUSING ASSISTANCE

1. Eligibility to receive benefits from a housing voucher program should be based on the condition of being "housing poor". This requires a different definition of eligibility than the standard income limits currently used.

   a. One method of defining "housing poor" which should be considered is based on a "market basket" approach. Available shelter income is computed by identifying the total income (after taxes) by household size left after subtracting the cost of meeting basic necessities for a minimum adequate standard of living as defined by the U.S. Bureau of Labor Statistics. Any household whose available shelter income is less than the amount of money needed to obtain standard quality accommodations for a household of its size should be considered eligible for housing assistance.

---

[1] This conclusion rests on the assumption that the low-income households most likely to apply for housing vouchers if the income limits for eligibility are not reduced would resemble the low-income households currently participating in the Section 8 Existing Program.

[2] Data obtained from the 1976 Annual Housing Survey indicate that 27% of the low-income households containing children live in substandard units, compared to 33% of the very-low income households with children.

   b. A reduction to 50% of median area income as a basis for eligibility to receive housing assistance cannot be endorsed because it eliminates household types (including large families and minorities) that are "housing poor".

2. Unless a "market basket" approach is adopted, procedures used to compute income for eligiblity determination should not be changed.

   a. Non-cash contributions from other forms of public assistance should not be included in the computation of income.

   b. Allowances for minors, higher than normal medical expenses, or other unusual expenses should be retained and the allowances for minors increased.

3. Households that receive assistance under a housing voucher program should continue to receive the subsidy as long as they remain eligible for the program.

4. Administrative funds must be made available to local units of government sufficient to enable affirmative efforts to ensure that all "housing poor" households can benefit, particularly large families and minorities. Proposals to reduce the amount of administrative funds allocated to units of local government should be rejected.

Chapter 4

PROBLEMS LIKELY TO RESULT FROM ELIMINATON OF PRODUCTION SUBSIDIES

I. BACKGROUND

The President's Commission on Housing has taken the position that the major housing problem confronting lower income households is no longer the shortage of rental housing or the prevalence of physically deficient units but the inability of lower income households to obtain decent accommodations at affordable prices. They reach this conclusion after an analysis of trends for the nation as a whole. The floor area per person in households has more than doubled in the last 30 years, overcrowding has declined by approximately 400% since 1940, and the percentage of dilapidated housing has declined from 50% in 1940 to less than 3% in 1979.[1] Approximately 7.5% of all housing units are rated as physically deficient in 1977 using an indicator of housing quality developed by the Congressional Budget Office. This represents a decline from 8.1% in 1975.

Contrasted to this decline in overcrowded and substandard housing conditions is the continuing increase in the proportion of households spending more than 25% of their income for housing. Approximately 51% of renters paid more than 25% of their income for rent in 1979, compared to 32% of the renters in 1950. Although it is clear that the inability to obtain decent accommodations without spending an inordinately high fraction of income is a serious and growing problem for lower income households, it is difficult to accept the argument that inadequate housing is no longer a serious problem deserving attention from the federal government.

The Commission's analysis reveals that deficient housing is still very prevalent among renters (13.3%), rural Southerners (12.8%), residents of large cities (9.6%), Blacks (19.1%), Puerto Ricans (12.3%), and female-headed households (10.1%).[2] Physically deficient housing may not appear to be a large problem when viewed in the aggregate. When viewed in distributional terms, however, poor quality housing constitutes a major problem for certain types of households and for certain areas of the country.

Although the Commission's Interim Report recognizes that some groups or areas are characterized by a greater concentration of inadequate housing than the nation as a whole, it nonetheless advocates termination of current housing production subsidies.[3] Instead, the Commission report presents preliminary recommendations that shortages of rental housing or the prevalence of poor quality housing, where they exist, be addressed by other means.[1] These include adding new construction as an eligible activity under the CDBG program; providing options for State and local agency financing of housing through tax-exempt or taxable bonds; changing federal tax policy to provide a tax credit for rehabilitation of residential buildings and encouraging private groups at the local level to sponsor and/or finance housing programs.

---

[1] This analysis is presented in Chapter 2 of the Commissions's Interim Report.

[2] The numbers in parentheses indicate the percentage of households in each group or area living in inadequate housing.

[3] The Commission's justification for this recommendation is two-fold. First, as indicated above, the primary housing problem of lower income households is identified as the affordability of housing, not the scarcity or inadequacy of the available housing. Second, the various production programs are very costly, both in terms of the per unit subsidy and the long-term financial commitment assumed by the federal government.

Clearly the Section 8 New Construction and Substantial Rehabilitation programs are very expensive ways to produce needed housing for lower income households.[2] At this time, however, it is uncertain that increased levels of new construction or substantial rehabilitation would be generated through the CDBG program or the issuance of state or municipal bonds.

Although the Commission correctly notes that many localities have made innovative use of their CDBG funds in rehabilitating properties, larger amounts of newly constructed or substantially rehabilitated rental units may not be produced through the CDBG program for a number of reasons. First, many localities have not used their CDBG funds to renovate multi-family rental housing.[3] As the Commission itself notes, more than 80% of the units funded through the CDBG program are single-family units. It is not apparent that localities will shift their emphasis to riskier multi-family rehabilitation just because the Section 8 supply-side programs are terminated.

Second, the proposed continuation of the annual funding cycle for CDBG is likely to limit the amount of new construction or substantial rehabilitation, since localities would be unwilling to incur long term financial obligations without assurance of continued federal support for a longer time period. The Office of Management and Budget's threat to eliminate the CDBG program entirely in Fiscal Year 1984 would certainly cause local officials to think twice about committing funds to these projects. Third,community development funds are being reduced at the same time that activities previously funded under HUD categorical programs are being folded into the program. With this increased competition for a reduced pot of funds, it is questionable that increased levels of new construction or substantial rehabilitation will be produced with CDBG funds.

It also seems unlikely, at least for the present, that municipalities or states will construct a significant volume of new rental units for lower-income households by issuing tax-exempt or taxable bonds. Conditions

---

1. The Commission indicated that it was very concerned about the shortage of adequate housing in specific areas and that it would continue to study housing supply problems in preparing its final report. That report could include recommendations for some type of rehabilitation or construction program.

2. A briefing paper prepared by HUD for the President's Commission estimatesthat a unit of Section 8 new construction costs approximately $100,000 tobuild. However, as Stegman demonstrates, a large part of the high cost of producing new or substantially rehabilitated units results from the desire to minimize short term budget impact by spreading the costs out over a longer time period. See Michael A. Stegman, "Housing Block Grants: Legislation Is Unlikely This Year", Journal of Housing, pp.317-324, June 1981.

3. Michael M. Ehrmann and Douglas Ford, "CD Rehabilitation: Analysis Reveals Dramatic Growth, Successful Local Programs", Journal of Housing, pp. 330-337, June 1981.

in the tax-exempt bond market and mortgage market currently are very unfavorable, with interest rates at the highest level in years, and municipal and state tax-exempt bonds are becoming less attractive investments to wealthy individuals because of the reduction in the maximum income tax rate. Furthermore, the future of tax-exempt bonds is uncertain, since the Treasury Department is opposed to the continued use of tax-exempt financing for housing. Even if tax exempt financing is continued, it is not clear that municipalities will use this mechanism to finance housing construction. They increasingly are recognizing the need to devote a larger share of the money raised through municipal bonds to infrastructure repair.

Finally, the reduced costs to the developer produced by tax-exempt financing will not be adequate to lower the rents to a level where they are affordable to lower income households without further subsidy. Given the higher rents charged for newly constructed units, the proposed reductions in the payment standard and the proposed maximum rent subsidy, it is unlikely that program recipients could rent a new unit without paying substantially more than 30% of their income for rent.

If these recommended solutions are not likely to eliminate a shortage of rental housing or rehabilitate physically deficient housing, is it likely that a housing voucher alone could do so? The answer, recognized in the Commission's Interim Report, is no.

> These programs (Section 8 Existing and EHAP) are less successful in reaching the poor who live in physically inadequate housing, and do not stimulate new construction or substantial rehabilitation (The President's Commission on Housing, 1981, p. 45).

Results obtained in evaluations of the Section 8 Existing Program supports this conclusion.[1] In the Section 8 Existing Program approximately 50% of the units that initially failed inspections were repaired. The percentage of rental units repaired after failing the initial inspection in the two supply sites of the Experimental Housing Allowance Demonstration was somewhat higher - 59% and 57%. In both programs, the repairs made were very modest. The housing analysts evaluating the performance of these programs concluded that the major impact of the programs on the housing stock is to promote maintenance and minor repairs, thus preventing further deterioration, but not increasing substantially the number of standard units through major rehabilitation. Units were upgraded generally only if the renovation costs were small.

The additional rent-paying ability of households with vouchers will not stimulate new construction, since they could not afford the newly constructed units even with the subsidy. For example, the median gross rent of units constructed between 1970-1976 in central cities in the U.S. was 1.22 times greater than the median gross rent for all units existing in 1970 ($202 vs. $165).[2] This disparity between the rent of

---

[1] U.S. Department of Housing and Urban Development, 1978; op.cit.; Abt Associates Inc., 1981, op.cit.

[2] Data presented in George Sternleib and James W. Hughes, America's Housing: Prospects and Problems (1980), p. 39.

Existing and new units is reflected in the different Fair Market Rent schedules for existing units and new construction/substantial rehabiliation units.

The foregoing analysis suggests that the supply of adequate housing is not likely to be increased substantially in localities if the current housing production subsidy programs are terminated unless they are replaced with other types of subsidy programs. If the eliminated supply-side programs are not replaced, households living in substandard housing at the time they are issued rent certificates or housing vouchers in tight housing markets or markets containing substantial amounts of deteriorated housing will experience great difficulty finding housing that meets program standards.

Insight into the difficulties likely to be encountered by households issued housing vouchers in a tight housing market can be obtained by examining the experiences of households issued Section 8 certificates in New York City during a period--January 1, 1979 to June, 1981--when the number of vacant units of standard quality was shrinking.

II. FINDINGS

New York City Has a Very Tight Housing Market.

Households in search of rental units in New York City are confronted with an extremely difficult and unenviable task - locating a unit of acceptable quality when the number of units vacant and available for rent represents only 2.13% of all occupied and vacant units and where those units that are available remain vacant for less than two months at the median.[1]

The difficulty of this task is further compounded for potential Section 8 or housing voucher recipients by the large number of rental units that would not meet program quality standards and by the high rents that exist in many areas of the city.[2] The large supply of poor quality units creates hardships for potential recipients for two reasons. First, households living in substandard units must move to receive the rent subsidy unless their unit is renovated. Second, the range of acceptable alternative units renting within the payment standard is reduced, thus making it harder for movers to locate a unit. This is a serious problem for two groups of potential

---

1. The data identifying the number of units vacant and available for rent are taken from the 1981 New York City Housing and Vacancy Survey conducted for New York City by the U.S. Bureau of the Census. The report analyzing the data has not been completed yet. However, a set of computer printouts containing the results of the survey is available for public inspection at the City of New York Municipal Research Library. The count of vacant units includes only those year-round rental units that are not dilapidated and are available for rent. The denominator used to calculate the vacancy rate includes all renter-occupied units plus the units that are vacant and available for rent. In February, 1981, there were 42,157 units vacant and available for rent and 1,933,887 renter occupied units.

2. The 1976 Annual Housing Survey indicates that 22% of all rental units failed Section 8 standards. The 1981 Housing and Vacancy Survey reveals that nearly 21% of all rental units have 3 or more maintenance deficiencies. These units probably would not meet Section 8 quality standards.

recipients - large households and minority households.[1] Minority residents also have the added disadvantage of possibly encountering discrimination when they try to move.

The restricted choice of housing available to renters in New York City has become even more limited during part of the time period covered by this study, as the vacancy rate has dropped from 2.95% in 1978 to its current level of 2.13%.[2] The competition for this dwindling supply of available rental units has increased during this period, as the median time that a vacant unit remained unclaimed decreased from 2.29 months in 1978 to 1.90 months in 1981. The increased competition for rental units has occurred simultaneously with a very slight increase in the total number of renter households. Not unexpectedly, rents have increased at the same time that the supply of adequate housing available for rent has become more scarce. Median gross rents for all renter-occupied units have increased by approximately 26% since 1978.[3]

Households Are More Likely to Become Non-recipients If They Have to Move to Receive Assistance

Under the able administration of the New York City Housing Authority, more than 30,000 households - 73% of those issued rent certificates - have benefited from participating in the Section 8 Existing Program since 1976, either by moving into decent quality or less crowded housing or by paying less of their own low incomes for rent. This is an impressive accomplishment, considering the limited number of available apartments and the poor quality of many of the rental units.

The high participation rate is attributable in part to two factors. As noted earlier, the majority of the City's Section 8 units were allocated to the elderly in the City's Housing Assistance Plan (HAP). Unlike other types of households, most of the elderly issued Section 8 rent certificates were eligible to receive the subsidy without moving.[1] This reflects the fact that elderly households in New York City are less likely than younger households to live in poor quality units. Second, in accord with HUD directives, a large number of the Section 8 certificates issued after 1979 represent conversion of assisted units from the Section 23 leased housing program to the Section 8 Existing Program. Households occupying these units became Section 8 recipients without moving.

---

[1] The 1981 Housing and Vacancy Survey indicates that 34.5% of Black households, 38.1% of Hispanic households and 12.5% of white households live in units with three or more maintenance deficiencies. Thirty-four percent of households containing five or more persons live in units with three or more deficiencies, compared to 15.6% of one person households.

[2] The vacancy rate in 1975 was 2.77. See Marcuse, Rental Housing in the City of New York: Supply and Condition 1975-1978 (1979) for discussion of changes in the rental housing market between 1975 and 1978.

[3] Data for 1981 were obtained from the 1981 New York City Housing and Vacancy Survey. The 1978 data were taken from the 1979 Marcuse study.

The effect of the tight housing market and the large incidence of deficient housing on households issued Section 8 certficates is revealed by two findings. First, the proportion of households that do not eventually receive Section 8 benefits after being issued certificates has increased at the same time that the vacancy rate and the length of time available units remain vacant has declined. Approximately 36% of households issued certificates after January 1, 1979 did not receive a subsidy, compared to 27% for the entire period between 1976 and 1981.

Second, households who wanted to move or who were required to move to receive the rent subsidy were substantially less likely to receive assistance than were households who were able to receive the subsidy without moving. Since the beginning of 1979, 80% of the non-recipients had to or wanted to move, compared to only 39% of the recipients. Looked at another way, approximately 54% of certificate holders who wanted to or had to move did not receive assistance, compared to only 15% of certificate holders who were eligible to remain in-place.[2]

The relationship between a household's wanting to or having to move to receive assistance and not receiving the subsidy is revealed very clearly in the experience of minority residents and households with children. Approximately 70% of households with children and Black and Puerto Rican certificate holders wanted to or had to move to receive the subsidy. (See

---

1. Eligible households that are offered participation in the program are issued certificates entitling them to a rent subsidy if they locate an apartment that is eligible under the program rules. A household in New York City can receive the subsidy in the unit it lives in when it receives the certificate if the following four conditions are met: (1) it pays 40% or more of its gross income for rent; (2) the unit meets the program quality standards or the landlord or tenant is willing to repair the unit; (3) the landlord agrees to participate in the program; and (4) the unit rent is less than or equal to the Fair Market Rent for a unit of that size. If any of these conditons are not met, a household must move to receive assistance. A household can choose to move even if the above conditions are met. (Because of the limited number of certificates available compared to the number of eligible households, households paying more than 40% of their income for rent and households living in physically deficient housing are given higher priority for participation than households living in standard housing and paying between 25% and 39% of their income for rent.) A household issued a certificate generally has two months to locate an acceptable apartment. If the household demonstrates that it is looking for a unit, it normally can obtain a two month extension. After the extension the certificate expires and is re-issued to another household.

2. Estimates of the characteristics of certificate holders were obtained by merging the sample of non-recipients with the data for recipients. See the Note on Data and Methodology at the end of this study for a discussion of this methodology.

Tables 2 and 3) More than 45% of the certificate holders in these groups did not eventually receive Section 8 assistance.

Minority households and families with children also were more likely than other households to occupy substandard housing, both in the total population of renters and among certificate holders who did obtain rental assistance. In a very tight housing market, the Section 8 Existing Program - and, by implication, the housing voucher program - appears to be more successful as an income transfer program than as a program to improve the housing quality of people living in substandard dwellings.[1]

The difficulties experienced by minority certificate holders in obtaining the rent subsidy underscores the continuing need for provision of a high level of support services by housing authorities administering the housing voucher program. The New York City Housing Authority is reputed to have a strong record of serving minority households, as the heavy minority presence in the public housing program attests. Furthermore, minority households are well represented (57%) among households issued Section 8 rent certificates. Although Housing Authority officials indicated that concerted efforts were made to help minority households find units, nearly 50% of minority households issued rent certificates dropped out of the program. Housing Authority officials believe this percentage would have been even higher had they provided less assistance to minority households.[2]

Although it is difficult for all households to find standard housing in tight housing markets, minority households generally experience greater difficulties than non-minority households for three reasons. First, since minority residents tend to live in the worst quality housing, it is likely that very little standard quality housing is available in their neighborhoods. Second, the awareness of minority households of available housing outside of minority neighborhoods is often limited, primarily because the information obtained through informal sources is restricted by the segregated housing markets prevalent in most cities.[3] And, third, discrimination in the housing

---

[1] This conclusion is based on two findings: (1) the percentage of certificate holders who did not receive assistance was more than three times as great among households who wanted to or had to move to receive assistance than among households who were able to receive the subsidy without moving; and (2) nearly all the recipients who moved lived in substandard housing when they entered the program. It should not be overlooked, however, that 34% of the households receiving the subsidy did move from substandard housing.

[2] Although comparisons are quite rough, it appears that the range of support services provided by the New York City Housing Authority is midway between the service levels provided by agencies described as offering a high level of services and the services provided by agencies described as offering a low level of services in tight housing markets in the administrative portion of the EHAP. Similarly, the proportion of minorities with certificates receiving the subsidy in New York City is midway between that achieved by EHAP agencies offering the highest level of services and the EHAP agencies providing the lowest level of services. This comparison possibly understates the effectiveness of the support services provided by the New York City Housing Authority because the vacancy rate is much lower in New York City than in the tight housing markets in the EHAP.

[3] See Raymond J. Struyk and Marc Bendick, Jr., editors, Housing Vouchers for the Poor, op. cit. p.124; and the President's Commission on Housing, Interim Report, op. cit., p. 39. for a discussion of these issues.

Table 2

Proportion of Non-Recipients Among Existing Section 8 Certificate Holders, 1979-1981

Household Group	Percent of All Certificate Holders Having to Move	Proportion of Certificate Holders that Are Non-Recipients
Single Non-Elderly	55.9%	33.5%
Single Elderly	39.6	30.0
One Adult w/Children	70.6	44.2
Two Adults w/Children	72.3	49.6
Two Elderly	39.8	18.5
Two Non-Elderly	62.6	51.0
Overall	53.7%	36.0%

Source: New York City Public Housing Authority Records

Table 3

Proportion of Certificate Holders Having to Move and Not Using Certificates, by Race/Ethnicity, 1979 - 1981

Household Group	Percent of All Certificate Holders Having to Move	Proportion of Certificate Holders that Are Non-Recipients
White	35.3%	22.8%
Black	68.9	46.9
Puerto Rican	69.5	47.6
Other Hispanic	54.4	38.5
Oriental	58.5	32.9
Other	52.5	0.0
Overall	53.7%	36.0%

Source: New York City Public Housing Authority Records.

market further impairs the ability of minorities to locate acceptable quality housing, especially if they must look for such housing outside of primarily minority neighborhoods.[1]

Maintenance of a high level of support services by local housing authorities to assist minority households overcome these barriers under either the Section 8 or housing voucher program will be very difficult if proposals to reduce the administrative fee are implemented.[2] Further economic or racial integration that might be encouraged by the Section 8 Existing Program or the housing voucher program would be jeopardized if housing authorities were forced to spend fewer resources helping interested minority residents find housing opportunities outside of their neighborhoods.

Many Households May not Have Received Benefits Due to the Inadequate Supply of Housing Meeting Program Standards.

Although households issued Section 8 rent certificates may not have received assistance for a number of reasons, the available evidence suggests very strongly that many of the households that did not receive the subsidy dropped out of the program because they could not find housing meeting program standards.[3] This is revealed most clearly in the experience of households containing children, since nearly half of these households issued certificates did not receive assistance.

Households with children issued Section 8 Existing rent certificates appear to have had a strong incentive to locate housing meeting the Section 8 standards, since the majority of these households lived in poor quality housing when they were issued rent certificates.[4] Furthermore, many of these households paid a greater share of their income to live in poor quality housing than previously was considered the maximum (25%) that could be spent without sacrificing non-shelter needs. More than half of the recipient households[1] with children who lived in substandard housing prior to entering the program paid more than 27% of their income for rent. (See the first column of Table 4)

---

[1] See Struyk and Bendick, op. cit., p. 127 for evidence that discrimination against minorities increases the costs and difficulties of finding an acceptable dwelling.

[2] It has been reported that HUD and OMB were proposing to reduce the administrative fee paid to housing authorities from 8.5% of Fair Market Rent (FMR) to 6% for each unit rented under the program. The reduction will be more than 2.5% in actuality since the FMRs used as the basis for calculating the administrative fee would also be rolled back under the HUD and OMB proposals (See The Congressional Record, op.cit.).

[3] See U.S. Dept. of Housing and Urban Development, Lower Income Housing Assistance Program (Section 8): Nationwide Evaluation of the Existing Housing Program (1978), pp. 45-55. for a discussion of reasons why households may not use their certificates. In addition to problems already discussed, households may not search for a unit very seriously or at all because they anticipate that they will not be able to locate a unit meeting the program standards. Households also may not receive assistance for a variety of personal reasons having nothing to do with the supply of housing. They may not want to move beyond the boundaries of their present neighborhoods and its attendant support networks, they may not be able to mount an effective search, they may not understand the program well enough to explain it to the landlord, or they may decide that the benefits offered by the program are not sufficiently large to offset the cost and inconvenience of moving.

[4] Fifty-five percent of recipient households containing two adults and children lived in substandard housing when they entered the program. Seventy-two percent of all housholds containing two adults and children issued rent certificates either had to or wanted to move to receive assistance. While some of these households may have lived in standard units, it is assumed that the majority did not.

Because larger households must spend a greater proportion of their income for non-shelter necessities,[2] these households face a more difficult tradeoff than other households between living in a minimally acceptable dwelling or maintaining a minimally acceptable level of consumption of other necessities. These large households thus may have been unable to rent standard quality units without a subsidy because they had less discretionary income to spend on housing after meeting their non-shelter needs.

The large households who lived in substandard housing prior to entering the program and who did find units that met program standards appear to have benefited substantially from the program. These families moved into large units that rented for considerably more than their previous units.[3] For example, households moving into three bedroom units obtained units that, at the median, rented for $145 more per month than their previous dwellings. (See the fourth column, Table 5)[4] Even though these families did not reduce their out-of-pocket rent expenses as much as households who remained in-place, the prospect of obtaining a better quality or less crowded unit by using their certificates appeared to be an important enough lure to convince these households to move.

Evidence presented earlier suggests that recipient and non-recipient mover households both tended to occupy substandard housing prior to applying for the

---

[1] Recipients are those households that received Section 8 Existing subsidies.

[2] See Michael Stone "Defining and Measuring Shelter Poverty", unpublished MS., (Boston: University of Massachusetts, 1981), p.9.

[3] It is important to recognize that the difference in gross rent between the unit rented under the Section 8 Program and the unit vacated is not a totally accurate measure of the improvement in housing quality. However, the nationwide evaluation of the Section 8 Existing Program found that mover households obtained dwelling units through the Section 8 Existing Program that rented for considerably more than pre-program units and that were significantly better in quality. See Abt Associates, Inc., Participation and Benefits in the Urban Section 8 Program, Volume 1, (Cambridge, Mass: January 1981).

[4] Data describing rent changes for households obtaining various size units are presented for two reasons. First, the possible effects of housing supply factors on household participation in the program are easier to see when focusing on unit size. And, second, households with children generally require the largest dwellings.

Table 4

Change in Rents for Households Receiving Section 8 Existing Assistance

Household Group		Median Pre-Program Rent/Income Ratio	Median Decrease in Tenant Rent Cost	Median Percentage Decrease in Tenant Rent Cost	Median Increase in Gross Rent of Unit	Median Percentage Increase in Gross Rent of Unit
Single Non-Elderly	Move	.579	$ 84	53.1%	$104	66.1%
	In-Place	.685	118	61.3%	11	5.7%
Single Elderly	Move	.472	58	43.3%	120	86.2%
	In-Place	.599	100	54.6%	20	8.5%
One Adult w/children	Move	.288	37	19.6%	119	61.2%
	In-Place	.532	151	56.8%	1	.5%
Two Adults w/children	Move	.276	31	16.0%	131	68.4%
	In-Place	.483	138	52.3%	6	2.4%
Two Elderly	Move	.432	76	40.7%	87	44.7%
	In-Place	.526	110	51.0%	14	5.9%
Two Non-Elderly	Move	.384	54	32.5%	97	56.2%
	In-Place	.530	114	51.8%	4	1.7%

Source: New York City Public Housing Authority Records

Table 5

Change in Rents for Households Receiving Section 8 Existing Assistance by Number of Bedrooms in Section 8 Unit

Number of Bedrooms		Median Pre-Program Rent/Income Ratio	Median Decrease in Tenant Rent Cost	Median Percentage Decrease in Tenant Rent Cost	Median Increase in Gross Rent of Unit	Median Percentage Increase in Gross Rent of Unit	Median Ratio of Pre-Program Rent to Fair Market Rent
0	Move	.469	$57	44.1%	$88	66.6%	.569
	In-Place	.579	97	55.8	30	1.7	.789
1	Move	.484	68	45.2	111	72.1	.594
	In-Place	.596	108	54.2	21	9.1	.800
2	Move	.286	33	18.0	121	65.8	.600
	In-Place	.517	141	53.9	4	1.3	.872
3	Move	.273	36	17.3	145	71.2	.563
	In-Place	.493	170	55.9	2	6.8	.860
4	Move	.254	38	20.0	166	79.0	.496
	In-Place	.463	183	59.0	9	2.4	.832

Source: New York City Public Housing Authority Records

program. If we assume that the recipient and non-recipient mover households are similar in other ways (and we have no reason to suspect this is not the case), then the non-recipient movers did not lack for incentives to use their certificates. The pattern of results - that large households are most likely to live in substandard housing prior to enrolling in the program, regardless of income, that these same households are more likely than other groups to be required to move to receive the subsidy, that they generally obtain units renting for substantially more than their previous inadequate unit when they do locate a unit, yet are the least likely of all groups to secure assistance under the program - suggests that many of these large households were not able to obtain units meeting Section 8 standards.

Two final pieces of evidence support this conclusion. First, even among certificate holders who are required to or want to move to receive the subsidy, households with children receive the subsidy less often than other households. And second, the vacancy rate is somewhat lower among units containing two or more bedrooms (2.04%) than among units with less than two bedrooms (2.34%).

In summary, many households have experienced difficulties obtaining rental assistance under the Section 8 Existing Program in New York City's tight housing market. Some types of households - especially minorities and households with children - have substantially less success than others using their certificates to obtain better housing. Although the evidence is not conclusive, it suggests that many households may have not participated in the program because of the scarcity of adequate housing meeting program standards. These households would face similar, if not worse problems, finding acceptable housing under a voucher program without some effort to expand the supply of standard housing for lower income households.

III. RECOMMENDATIONS REGARDING CHANGES IN HOUSING SUBSIDY PROGRAMS

1. A housing voucher program for lower income households is endorsed only if there are sufficient production programs to ensure that standard housing is available and maintained for "housing poor" households.

   a. Those housing production programs which provide standard housing at the lowest cost primerily to the "housing poor" should be emphasized. Production programs that are shown to benefit "housing poor" households should be funded.

   b. Housing production programs should be targeted to areas with a demonstrated shortage of standard housing for "housing poor" households. Examples of indicators signifying a need for the production programs are a low rental vacancy rate and a short vacancy duration or the existence of a large supply of substandard housing.

   c. Where adequate programs to increase the supply of standard housing for "housing poor" households in differing circumstances do not exist, they should be created. Examples of such programs are: direct production subsidies, deferred-second mortgage home purchase, improved operating subsidies for public housing, revised tax provisions to encourage maintenance of present rental housing stock, conversion of homeowner deductions to credit, subsidies for mutual housing associations or limited equity cooperative, and additional subsidies for lower income home-ownership.

2. In addition to necessary federal involvement, proposals to encourage private foundations, labor unions, corporations and religious institutions to provide housing and to enhance the use of pension funds for housing investment are endorsed. However, these proposals cannot be expected to have any significant effect on the production of housing units for lower income people.

3. Preservation of the existing stock of publicly assisted housing must be a priority.

Chapter 5

THE EFFECT OF CHANGES IN THE PAYMENT STANDARD USED TO CALCULATE HOUSEHOLD SUBSIDIES

I. BACKGROUND

Current Procedures Used to Calculate Household Subsidies

Under the Section 8 Existing Housing Program, a household is permitted to live in a standard quality unit of its choosing as long as the unit rent does not exceed a maximum rent, called a Fair Market Rent (FMR), which varies by unit size. The household cannot participate in the program if it occupies a unit whose rent exceeds the FMR for a unit of that size. The schedule of rents was originally set by HUD for each SMSA in the country so that the rents of half of the recently vacated units in the SMSA meeting the program quality standards would fall below the FMR schedule. Local housing authorities (PHAs) were given the authority to approve rents within 110% of the FMR for a maximum of 20% of the households receiving Section 8 assistance. In addition, the PHAs could petition HUD for permission to rent a greater percentage of units within 110% of the FMR or could seek upward revisions in the entire schedule. The schedule of FMRs for each SMSA has been revised a number of times since the program's inception in 1975.

In contrast, households in the field trials of the housing allowance experiment (EHAP) were permitted to rent units in excess of the FMR. In that situation, households' rent contributions were determined by calculating the difference between the FMR and 25% of the households' adjusted income, with the households paying the entire portion of the rent in excess of the FMR.

The effect of the FMRs on restraining or increasing program costs has been debated since the start of the program.[1] The disagreement has centered on four questions. Does the FMR restrict households' choices to a limited range of neighborhood and housing types? Second, does the rent ceiling embodied in the FMR schedule encourage landlords to raise their rents to the maximum allowable rent? Third, are the FMRs set at a level which is higher than the rent required to obtain a unit just meeting the Section 8 quality standards? And fourth, have the increases in the FMRs since 1975 exceeded the rate of increase in market rents during the same period?

Evidence addressing the last three questions is available at the national level. A comparison of the rent increases of households participating in the Section 8 Existing Program and the Experimental Housing Allowance Program suggests that landlords were encouraged by the Fair Market Rents to raise their rents. Households using the Section 8 certificates to lower their rent/income ratio in their already standard units experienced a 26% rent increase in the Section 8 program, compared to a 4% increase in the supply experiment component of EHAP. Movers experienced a 52% increase in rents in the Section 8 Program and a slightly lower 34% to 45% increase in EHAP.[1] According to the study conducted by Olsen and Rasmussen, Fair Market Rents are set somewhat higher than the average rent of units just meeting Section 8 standards and have increased at a greater rate than the market rents in most SMSAs.[2]

---

[1] For an excellent discussion of the issues involved, see Jill Khadduri and Raymond J. Struyk, "Improving Section 8 Rental Assistance", Evaluation Review, Vol. 5, 1981; Edgar O. Olsen and David W. Rasmussen "Section 8 Existing: A Program Evaluation", Dept. of Housing and Urban Development. Occasional Papers in Housing and Community Affairs, Volume 6, 1980.

Proposed Changes in Procedures Used to Calculate Household Subsidies

The President's Commission has recommended that an approach similar to that used in the EHAP be adopted. A household would be free to occupy a unit renting for more than the standard used to calculate the tenant contribution, with the tenant required to pay the difference between the rent and the standard.[3] In other words, the voucher recipient would pay more than 30% of his/her income for housing if the unit rent exceeded the payment standard. Conversely, if a standard unit renting for less than the payment standard were found, the recipient could pocket the difference.

In December 1981, the Department of Housing and Urban Development and the Office of Management and Budget were reported to have proposed changes in the way the payment standard is calculated. HUD proposed one major change - using as the payment standard the 40th percentile rent, instead of the median rent. The base upon which the standard is computed - all recently vacated units in the SMSA meeting the quality standards - was not changed.[4] The OMB proposed three major changes; (1) using the 40th percentile; (2) excluding newly built units from the calculation; and (3) including in the calculation all existing units meeting the standard, not just those recently vacated.[5]

Implementation of the HUD proposal obviously would result in a lower payment standard. Adoption of the OMB proposal would produce an even lower payment standard for two reasons. First, dropping new units excludes higher rent units from the calculation, since the rents of new units generally exceed those of existing units. Second, including all existing units, not just recently vacated ones, adds to the calculation many units where the rents charged long-term occupants are lower than the rents that would be charged to new tenants if the units are vacated.[1]

---

[1] Khadduri and Struyk, 1981, p.197.

[2] See Olsen and Rasmussen, op.cit.

[3] The phrase payment standard is used to refer to the standard to be employed in both the Section 8 Existing Program and the housing voucher program to calculate households' rent contributions. The changes referred to in this section reflect HUD and OMB proposals made public as of December 21, 1981.

[4] The 40th percentile represents the rent at which 40% of the standard quality units could be rented. The median represents the level at which 50% of the standard quality units could be rented. Dropping the cutoff from the median to the 40th percentile means that 20% of the units that previously were accessible to Section 8 recipients will no longer be available unless renters are willing to spend more of their income for rent than is required by the program.

[5] The description of these proposals in the Congressional Record indicates that the changes were intended to take effect in Fiscal Year 1983. In addition, HUD was also reported to have proposed, with OMB approval, reducing the Fair Market Rents for Fiscal Year 1982. The details of the proposed FY 1982 reductions were not specified. (See The Congressional Record, December 7, 1981, op.cit.)

If length-of-tenure discounts are common in an area, rents of units that have not recently experienced a change in occupancy will be lower than the rents that would be charged households using their certificates to move to new units. As a result, the rents of these units will underestimate the rents that voucher recipients would have to pay if they moved.

The analysis presented in this chapter was completed before the HUD and OMB proposals were released. In addition, we do not have the data needed to estimate the payment standards that would be produced for New York City if the preliminary HUD and OMB proposals are implemented. Instead, this chapter estimates the effect on the current Section 8 recipients of adopting a payment standard that is 10% lower than current Fair Market Rents. The proportion of recipients who would have to pay a greater fraction of their income for rent under such a standard is identified. Estimates also are made of the proportion of their income that program recipients would have to pay for rent in their Section 8 unit if the housing voucher payment standard is 10% below that of the Fair Market Rent for their unit.

Some perspective would be helpful in evaluating the findings presented below. The key question, obviously, is how does the 10% reduction in the FMRs used in this analysis compare to the reductions in the payment standard likely to result from the HUD and OMB proposals. Although the comparison is rough, it appears that the HUD and OMB proposals would reduce the payment standard by more than 10%. A reduction of 15% to 20% seems a reasonable guess.[2] As a result, the findings presented below can be interpreted as reasonable, if not somewhat conservative, estimates of the impacts likely to result from the reported Administration proposals to reduce the payment standard used to calculate program recipients' rent contributions.

---

[1] The difference between the rent charged a long-term tenant and the rent that a new occupant would pay is often referred to as a "length-of-tenure" discount.

[2] This estimate was arrived at in the following manner. The FMR for a two bedroom unit in New York City in 1981 is $407/month, including utilities. A 10% reduction brings the FMR down to $366/month. Median and 40th percentile rents were estimated for 2 bedroom units from the 1981 Housing and Vacancy Survey conducted in New York City. All rental units except old-law tenements and rent controlled apartments were included in the calculations. Old-laws were excluded because they do not meet current quality standards; rent-controlled units were excluded because a unit is decontrolled when it is vacated and the current rents are very unrealistic estimates of the rent levels facing program recipients when they look for a unit.

The median and 40th percentile gross rents per room were multiplied by 4.5 rooms (the number of zoning rooms in a 2 bedroom unit) to obtain the estimated median ($380/month) and the 40th percentile rents($340/month) for 2 bedroom units. These estimates probably are lower than those that would be obtained using the proposed HUD procedure because approximately 15-20% of the units included in the calculation would not pass the quality standards and because units are included that have not been recently vacated. On the other hand, these estimates probably are somewhat higher than those that would be produced using the OMB procedure.

II. FINDINGS

Many of the households (20%) that have received assistance under the Section 8 program obtained units whose gross rents under the initial lease exceeded Fair Market Rents for those size units (See Table 6).[1] Another 10 percent of the recipients occupied units with rents equal to the FMR. Approximately 43% of the recipients occupied units with gross rents less than 90% of the Fair Market Rent.

Dropping the payment standard 10% below Fair Market Rents would force a substantial number of Section 8 recipients to pay more of their income for rent, if such a change were applied to current program participants. The 30% of the recipients living in units already renting at or above the Fair Market Rent clearly would have to pay more than 30% of their income for rent. In addition, some of the recipients whose unit rents are within 10% of the Fair Market Rent would be affected by this change. A reduction in the payment standard would fall rather hard on these households, since their rent contribution is already being increased from 25% to 30% of their income.[2]

Estimates of the median rent-to-income ratio likely to be paid by households receiving Section 8 assistance if the payment standard is lowered 10% are presented in Table 7. The impact on all household groups is quite dramatic. For example, half of the very low-income single elderly households would have to pay more than 34% of their income for rent; one-fourth of these same households would have to pay more than 39% of their income for rent.[3] The impact would be equally as severe for very low-income households containing one adult and children.

The data presented in Tables 6 and 7 document quite clearly that, at least in New York City, a 10% reduction in the payment standard would exacerbate the very problem - housing affordability - that housing vouchers are designed to alleviate. If the roll-back in FMR levels proposed for Fiscal Year 1982 is not applied to current recipients, the changes obviously would affect only households coming into the program after the start of the 1982 Fiscal Year.

The impact on future program participants depends upon how closely the current Fair Market Rents reflect the rents actually charged for dwellings meeting the program quality standards. Again, precise estimates are not possible because of data limitations. The rough comparisons that are possible suggest that the FMR for a two bedroom unit ($407) is similar to the median gross rent ($380) for a similar size unit calculated from the 1981

---

[1] The gross rent and Fair Market Rent maintained in the New York Housing Authority's files for each household receiving assistance in the Section 8 Program are the gross rent for the unit agreed upon in the initial lease and the Housing Assistance Payment Contract and the Fair Market Rent for the size unit listed on the Section 8 certificate. The analysis assumes that the Fair Market Rents for various size units have not increased faster than the gross rents of the units. This does not appear to be an unreasonable assumption.

[2] The proportion of recipients' income paid for rent is currently being increased 1% per year until it reaches 30%. Under the OMB proposals, the increase to 30% would occur in 3 years instead of 5.

[3] The 75th percentile indicates that 25% of this group would have rent-to-income ratios greater than the value for the 75th percentile.

Table 6

Percent of Recipient Households by the Ratio of Contract Rent in Section 8 Unit to Fair Market Rent

Ratio of Contract Rent to Fair Market Rent	Total
.001 - .399	0.0%
.4 - .699	7.7
.70 - .799	14.3
.80 - .899	20.4
.90 - 1.0	37.2
1.01 - 1.0499	4.2
1.05 - 1.099	13.3
1.10 and over	2.9
Total	100.0%

Source: New York City Public Housing Authority Records

Table 7

Estimated Rent/Income Ratio of Households Receiving Section 8 Assistance if Payment Standard is Set at 90% of Current Fair Market Rent Schedule, by Household Type and Income Level.[a]

	Very Low-Income		Low-Income	
Household Type	Median Rent/ Income Ratio	Rent/Income Ratio at 75 Percentile	Median Rent/ Income Ratio	Rent/Income Ratio at 75 Percentile
Single Non-elderly	.355	.422	.343	.387
Single Elderly	.346	.390	.345	.385
One Adult w/children	.343	.393	.345	.372
Two Adults w/children	.346	.382	.340	.360
Two Elderly	.333	.374	.356	.394
Two Non-elderly	.334	.375	.345	.386

[a] Calculations are based on the assumption that households would be required to pay 30% of their income for rent in the absence of a reduction in the payment standard.

Source: New York City Public Housing Authority Records

New York Housing and Vacancy Survey according to the procedure described earlier.[1] These two rents would be more similar if the median rent obtained from the Housing and Vacancy Survey were calculated in the same manner as the Fair Market Rent.[2] Even if the $380 figure is the most accurate estimate of the median cost of minimally acceptable housing, reducing the payment standard to the 40th percentile rent ($340/month) undoubtedly still would make it more difficult for households issued certificates or vouchers to locate standard quality housing renting below the payment standard in New York City's tight housing market. Of course, they would be free to secure a unit whose rent exceeds the payment standard, not so much out of choice but for lack of less costly alternatives. In such a situation, the voucher again would have failed to achieve its major purpose - alleviating the rent burdens faced by many lower income households.

The ability of future participants to locate standard housing within the payment standard may be further hampered if the reported decision by HUD to limit future increases in the FMR to 5% a year is implemented. If future rent increases resemble those of the past three years, this permitted rate of increase would not even keep pace with the increase in rent levels in New York City. Median gross rents for all renter occupied units increased by approximately 26% since 1978, an annual rate of increase of 8.7%. If this trend continues, the cost of standard quality housing will steadily rise beyond the ability of program participants to afford it.

The proposed reduction in the payment standard may have another negative impact on households receiving a voucher or rent certificate. A lower payment standard will restrict the housing choices that potential recipients can afford, even with a subsidy, and probably will reduce the number and variety of neighborhoods in which these choices are located.[3] The opportunity for racial or economic integration created by the Section 8 Existing Program, even if little used in the past, will be threatened by the reduction in the payment standard.

III. RECOMMENDATIONS REGARDING CHANGES IN PAYMENT STANDARDS

1. The payment standard used to calculate rent subsidies must be adequate to allow eligible households to occupy decent housing of an appropriate size in the market area without paying excessive proportions of income for housing costs, including utilities.
    a. The median rent of all recently occupied dwelling units, including newly constructed units, should be retained as the payment standard.
    b. Any proposal to reduce the payment standard should be opposed because it will increase the difficulty of finding suitable available housing at reasonable costs.

---

[1] See footnote 2, page 43.

[2] That is, by excluding units that would not meet the quality standards and units that were not recently vacated.

[3] Whether or not a reduction in the payment standard reduces the range of neighborhoods in which recipients can afford to rent units depends upon the spatial distribution of rents in each locality.

   c. Changes in the payment standard should keep pace with changes in the cost of obtaining standard housing in each locality.

   d. The amount of funds budgeted per voucher should be adequate to ensure that households are not forced into paying excessive proportions of their income for housing costs in order to find standard housing.

2. Households should not be required to pay more than 25% of their income for housing costs, including utilities.

   a. Non-cash contributions such as food stamps should not be included as income for purposes of computing program recipients' rent contributions.

   b. Income allowances for minors and deductions for higher than normal medical expenses or other unusual expenses should be retained.

3. If households obtain units renting for less than the payment standard, they should be allowed to keep the difference between the payment standard and the actual rent of the unit as an incentive to keep housing costs down.

4. Households should be allowed to obtain units costing more than the payment standard if they are willing to pay the excess costs themselves.

   a. However, this approach is viable only if the payment standard is reasonable and there is an adequate supply of standard housing available in the market area.

   b. Any attempt to use this provision to compensate for an unreasonably low payment standard must be rejected.

Chapter 6

THE EFFECT OF QUALITY STANDARDS ON HOUSEHOLDS AND NEIGHBORHOODS

I. BACKGROUND

Previous sections of this report have examined the potential impact of program changes on the "housing poor". Data were collected and analyzed to determine the effects on the potential benefit population of changes in eligibility criteria and elimination of housing production programs, among others. In this chapter, the focus turns to the potential impact of the quality standards used in the program on the choices of potential recipients and on neighborhood viability and to the role of neighborhood groups in the voucher program.

The data relied upon in this chapter come from interviews with representatives of neighborhood organizations in New York City who work with the housing poor. They have observed the impact on neighborhood residents of the Section 8 Existing Housing Program, one of the programs which has served the housing needs of the poor in New York City.

One of the most popular aspects of a housing voucher program, and of the Section 8 Existing Housing Program, is the flexibility offered to recipient households. Households with a rent certificate or a housing voucher generally have the choice to stay where they are or move to a different, better, or larger unit. Also, if they want to move to a different neighborhood, theoretically they can exercise that choice.

Neighborhood groups in New York City, however, feel that the freedom of choice provided by the Section 8 Existing Program and a housing voucher program is illusory for many lower income households. Rather, they feel that these programs may contribute to the displacement of households from neighborhoods. As we observed in Chapter 4, households often are required to move in order to benefit from the Section 8 Existing Program. This usually occurs because their dwelling units fail to meet program standards and landlords are unwilling or unable to make the necessary repairs. This also would occur under a housing voucher program if similar housing quality standards are adopted.

This situation poses a difficult dilemma for potential beneficiaries and creates problems for households and groups in lower income neighborhoods that are trying to upgrade the quality of neighborhood housing. If most of the available housing in these neighborhoods is of poor quality, certificate holders or voucher recipients must choose between remaining in their neighborhood or receiving the rent subsidy.

The problem created for some neighborhoods by the imposition of standards resembling those of the Section 8 Program is that the inability of neighborhood residents to use their rent certificates or housing vouchers in the neighborhood perpetuates the inability of neighborhood renters to pay the higher rents necessary to maintain neighborhood properties.[1] Thus the application of strict quality standards may restrict the housing choices of potential recipients. And, by eliminating much of the housing in certain neighborhoods from consideration, it may hamper the ability of residents or groups in these neighborhoods to improve the quality of neighborhood housing.

Very few persons are likely to disagree with the policy of requiring that households live in standard quality units in order to receive the rent subsidy. The issues around which people may disagree, though, are the definition of what constitutes acceptable or standard quality housing and the range of flexibility permitted in enforcing this definition.[2] These are important questions, since the results of the EHAP demonstration indicate that the strictness of the standards affects the participation of households in the program. The proportion of households that eventually receives the subsidy decreases as stricter standards are adopted. Furthermore, those households that tend to live in poor quality housing - minorities and large households - are most adversely affected by adoption of strict standards.[3]

Under the current Section 8 Existing Program, the Department of Housing and Urban Development has specified a set of Performance Requirements and Acceptability Criteria to which units occupied by Section 8 recipients must conform.[4] Although these Performance Requirements and Acceptability Criteria are quite detailed, a certain amount of flexibility in interpretation is permitted. Localities can request HUD approval to tailor the standards to meet unique local circumstances. In addition, some of the Performance Requirements and Acceptability Criteria allow considerable room for judgement in deciding whether or not a specific property meets the standards. For example, the Acceptability Criteria used to evaluate the adequacy of the neighborhood in which a Section 8 recipient wants to rent a unit are:

> The site and neighborhood shall not be subject to serious adverse environmental conditions, natural or manmade, such as dangerous walks, steps, instability, flooding, poor drainage, septic tank back-ups, sewage hazards or mudslides; abnormal air pollution; smoke or dust; excessive noise, vibration or vehicular traffic; excessive accumulations of trash; vermin or rodent infestation; or fire hazards (24 CFR 882.109 (K)(2)).

---

[1] Findings presented in the evaluations of the Section 8 Existing Program and the EHAP demonstrations indicate that Section 8 Existing subsidies and housing allowances do not stimulate major rehabilitation of substandard units. Slight upgrading of units was observed if the cost of the repairs was minor. The major effect of the programs was to prevent future deterioration by enabling tenants to pay rents that supported maintenance of the units. Section 8 subsidies and housing vouchers may facilitate major upgrading of buildings if they are combined with rehabilitation financing provided by the CDBG program.

[2] It must be noted that the representatives of neighborhood groups interviewed and the officials administering the Section 8 Existing Program in New York City differ in their views regarding the stringency of the standards that should be adopted and the flexibility with which they are administered.

[3] See Raymond J. Struyk and Marc Bendick, Jr., editors, Housing Vouchers for the Poor, op. cit, Chapter 8, and Department of Housing and Urban Development, Experimental Housing Allowance Program, Conclusions, The 1980 Report, op. cit, p 9.

[4] See 24 CFR 882.109.

While the criteria against which neighborhoods are to be evaluated are identified, decisions regarding what is considered "serious", "adverse", "excessive", "abnormal" etc. are left to local officials. Furthermore, local officials can request HUD approval to change specific Performance Requirements or Acceptability Criteria if they believe the standards create hardships for the locality.

The President's Commission on Housing has recommended that housing voucher recipients be required to occupy standard housing. Although they did not specify the content of the standards, they suggested a number of factors which should be considered in adopting the standards:[1] (1) they must insure the health and safety of the recipients; (2) they should not be set so low that recipients do not obtain decent housing; (3) they should not be set so high that meeting the standards requires an excessively high subsidy; (4) because of varied housing market conditions in localities throughout the U.S., local standards, subject to basic national criteria, are preferable to federal standards if they meet the first three conditions; and (5) local standards should not inhibit access to any area in a locality.

While recognizing the importance of requiring voucher recipients to occupy standard units, these recommendations seem to permit a substantial amount of local flexibility in selecting quality standards.[2] However, the reported Administration proposal to reduce the administrative fees paid to local agencies may have an adverse effect on the maintenance of whatever standards are adopted. Officials in the New York City Housing Authority believe that the annual inspections made to units occupied by Section 8 recipients ensure that the units are maintained properly. The reduced funding for administrative functions may threaten the ability of local agencies to perform annual inspections.

The remaining three sections of this chapter discuss the neighborhood groups' perceptions of some of the problems that result from administration of the current Section 8 standards and that are likely to exist under a housing voucher program unless more flexible standards are used; propose some ways in which adoption of flexible standards might better suit the needs of lower income households and neighborhoods; and suggest that the viability of lower income neighborhoods could be enhanced by providing roles for neighborhood organizations in the voucher program.

II. FINDINGS

The Administration of Current Housing Quality Standards May Overlook Important Opportunities for Obtaining Standard Housing

Not all households that are eligible to obtain a housing voucher live in the same kind of situation. As we have seen, many households need assistance in reducing the proportion of their income they pay for housing costs, others need larger housing units, and some live in otherwise substandard units and need a better quality unit.

---

[1] The President's Commission on Housing, Interim Report, op. cit, p. 41.

[2] The preliminary HUD and OMB proposals contained in The Congressional Record do not identify their positions regarding the types of housing quality standards to be used in the housing voucher program or the continued Section 8 Existing Program.

Within this range of circumstances exists a wide variety of living conditions that can be used to meet the housing needs of lower income households. Throughout the country, and indeed in New York City, efforts are underway to utilize conversions, sweat equity programs, other rehabilitation efforts and alternative management schemes to increase housing opportunities for lower income households.

Clearly it is important to impose standards of health, safety and livability for housing units in which program beneficiaries live. No one interviewed endorsed the possiblity of slum-landlords receiving Section 8 or voucher payments while renting substandard apartments to lower income families unable to afford a decent place to live.

However, those interviewed indicated that many apartments that are important and unique housing opportunities for lower income families do not meet the standards currently used in the Section 8 Program. They expressed concern that a program providing housing assistance would require a family to move from these units in order to receive the benefits of that program if they did not want to move.

As we observed in Chapter 4, many of the households who move in order to receive the rent subsidy drop out of the program. Undoubtedly, many of these households cannot find suitable or acceptable units within the Fair Market Rents. But it is also undoubtedly true that some of these households elect not to receive benefits from the program if it means that they must leave their neighborhood or their building in order to do so. Some of these households might not have to make this choice if they are allowed greater flexibility in how they can use their certificate or voucher.

Two types of units that currently do not meet Section 8 quality standards seem to offer important housing opportunities for lower income households. The first are the old-law tenements that exist predominantly in certain sections of the City. The Lower East Side and Clinton, for instance, have vast numbers of these pre-1879 five story walk-ups. These tenements serve, by and large, lower income families, many of whom have lived there for generations and who find within a few blocks all that is necessary to sustain them.

Most old-law tenements do not have three piece bathrooms (a sink, toilet, and a bathtub) all within the apartment. This violates the Section 8 Program quality standards.[1] Most old-law tenements also have some rooms without windows. Since windowless rooms cannot be counted toward the total room count, these apartments can only qualify if their rent is less than or equal to the Fair Market Rent for a smaller apartment. The structural and lay-out alterations required to provide each apartment with a three piece bathroom instead of a toilet down the hall and to remove walls to rid an apartment of its windowless rooms are substantial and costly.

---

1. The Section 8 Acceptability Criteria specify that "a flush toilet in a separate, private room, a fixed basin with hot and cold running water, and a shower or tub with hot and cold running water shall be present in the dwelling unit, all in proper operating condition." 24 CFR, Part 882, 109 (a) (2). It appears that all three pieces must be located in the same unit, but that only the toilet must be located in a separate, private room.

Yet many, although certainly not all, of these apartments are otherwise suitable in terms of health, safety and livability. They are clearly providing much needed housing for lower income families in New York City. At best, the situation presents a two-edge sword. Some of those interviewed felt that the Section 8 Existing Program and housing voucher standards could be altered to accommodate those old-law tenements which are suitable in all respects except for the structural characteristics that do not currently meet the Section 8 Existing standards. Yet, at the same time, the persons interviewed recognized the importance of providing decent and suitable housing for lower income households.

The second type of unit presently not meeting the standards required for approval in the Section 8 Program are many of the apartment buildings being managed and operated by alternative managing agents or the tenants living in the building. By the time these units are abandoned, they are, in most instances, in such poor condition that they cannot qualify for the Section 8 Existing Program.

In these instances, it is indeed true that the units do not meet standards of health, safety and livability. The tenants nonetheless are often willing to pay restructured rents to finance the necessary repairs and maintenance of the building if they can obtain Section 8 Existing rental asssistance. However, because the apartments do not qualify for the Section 8 Existing Program without the repairs, the tenants cannot afford the rents required to allow them to make such repairs and operate the building adequately. In these instances, the tenants are not really given a chance to turn the building around.

Many non-profit neighborhood groups have saved many buildings and helped tenants in troubled neighborhoods. They have encountered situations where the tenants of an abandoned building were willing to assume the responsibility of managing and renovating the building only to discover that they were ineligible for Section 8 because the apartments did not yet meet the quality standards.

One suggestion offered is that in those circumstances where abandoned buildings are being managed by tenants or other responsible indiviuals or groups, households be allowed to benefit from the Section 8 Existing or housing voucher program on the condition that the apartment is brought up to program quality requirements within an agreed upon time period.

Another suggestion is that tenants be allowed to exercise flexibility in their use of Section 8 Existing certificates and housing vouchers so that they do not forfeit housing opportunities that they desire. Two examples of such circumstances are: instances where a building is converted into cooperatives or condominiums and instances where tenants are using rents to operate the building, finance required repairs or negotiate with the landlord for repairs. Again, these households could be allowed to use their certificate or voucher under the stipulation that the unit or building meets the standards within a specified time period. In each instance, the situation may represent an important housing opportunity and a means by which housing needs can be met without requiring the program recipient to move from the unit and, possibly, the neighborhood.

Certain Neighborhoods Can Be "Redlined" and "Triaged" by Requiring Households to Move to Receive Program Benefits.

While the administration of the current Section 8 Existing housing standards ensures that households benefiting from the program live in good quality housing, this otherwise desirable aspect of the program may have the unintended effect of "redlining" buildings and neighborhoods. Virtual "triage" could result from households being required to move to receive the subsidy when their landlords are unwilling to bring the unit up to standards. In reality, limiting a household's choice to staying in its dwelling unit or moving to participate in the program contradicts the stated intention of providing freedom of choice to potential beneficiaries.

According to interviews with neighborhood groups, such an outcome could occur for two reasons. First, the neighborhood might contain a predominance of buildings, such as old-law tenements, that are basically sound structurally but which do not meet other program standards. Second, the neighborhood might contain a substantial percentage of buildings that are deteriorated. In the absence of funds to rehabilitate the properties, the households would not be able to participate in the program and remain in the neighborhood. These situations also would occur under a housing voucher program if quality standards similar to those in the Section 8 Existing Program are adopted.

Neighborhood groups are concerned about the future viability of neighborhoods where much of the housing stock does not meet the Section 8 quality standards. The representatives interviewed felt that these neighborhoods suffer when households are required to move to receive housing assistance.

Yet, no one interviewed expressed an interest in devising a program that would enable otherwise ineligible families to participate in the program or that would restrict the freedom of households to use the rent certificate or housing voucher to move to another neighborhood. Rather, they believed that efforts should be made under the voucher program, in as many situations as possible, to enable a family to receive the subsidy in its unit if that were its choice. Furthermore, they felt that it was important to recognize that the Section 8 Existing Program has been designed in such a way that the stability and cohesiveness of a neighborhood are not necessarily taken into account in the issuance of certificates. There is no indication yet that the housing voucher program will place greater emphasis on maintaining neighborhood stability.

Clearly, this is an important concern, since no housing program should disrupt neighborhoods. An early evaluation of the Section 8 Existing Housing Program, however, concluded that the program did not appear to threaten the stability of neighborhoods. The study examined the possiblity that the program might contribute to neighborhod instability in at least two ways.[1] The first is the increase in demand for housing as a result of the improvements taking place in the neighborhood. This could cause displacement among eligible households who are unable to obtain certificates because of limited program funds. The second is that program subsidies could induce recipients to move out of the worst housing and neighborhoods, causing their accelerated abandonment and decline.

---

[1] Edgar O. Olsen and David W Rasmussen, "Section 8 Existing: A Program Evaluation", Occassional Papers in Housing and Community Affairs, (Washington, D.C. HUD, December 1979), Vol. 6, pp. 1-32.

Relying on findings obtained from the EHAP demonstrations, Olsen and Rasmussen concluded that the Section 8 Existing Program is not likely to have either of these effects, even though there is a slight tendency for recipients to move from the poorest areas.[1] Moreover, they suggested that, at worst, the Section 8 Existing Program contributes to neighborhood instability only in the long-term through increased movement from distressed neighborhoods. The small size of the program, however, led them to conclude that such an impact is not likely to be very significant.

The results of the Olsen and Rasmussen study, though, do not invalidate the perceptions of neighborhood groups that requiring a household to move from substandard units to receive the subsidy undermines the stability of the neighborhood. The social and economic viability of even a single building can be jeopardized if a few households must leave the building to participate in the housing voucher program. The increased instability perceived by neighborhood groups may occur on a small scale or gradually over time and might never be reflected statistically in an examination of changes in neighborhood stability. But the change is no less real to neighborhood residents.

A related concern of neighborhood groups is that greater emphasis should be placed on using housing vouchers to strengthen neighborhoods. Neighborhoods could be strengthened in two ways. First, lower income residents can be subsidized to remain in standard units they can no longer afford. As we observed in Chapter 4, this is happening in New York City. Second, as discussed in the previous section, households can be allowed to take advantage of important housing opportunities that do not currently meet the quality standards if they agree to meet the standards within a specific period of time. In each situation, the assurance of a steady, adequate cash flow would enable landlords to maintain the units, thus preventing further deterioration. The study by Olsen and Rasmussen, however, suggests that neighborhoods are not likely to be strengthened under current funding levels unless housing vouchers or Section 8 Existing funds are targeted to specific neighborhoods.[2] In largely deteriorated neighborhoods, though, even targeting rent certificates or vouchers would not allow potential beneficiaries to remain in the neighborhood unless rehabilitation efforts also were focused on the neighborhoods.

These two issues - the nature and flexibility of the quality standards adopted and the ability to target vouchers to deteriorated neighborhoods by linking them with rehabilitation efforts - must be considered carefully in designing the housing voucher program. The restrictiveness of the standards becomes an even more crucial issue if, as the President's Commission on Housing recommends, current housing production subsidies are eliminated. Without production subsidies or the ability to target vouchers to neighborhoods being rehabilitated under the CDBG Program, adoption of strict standards will make it very difficult, if not impossible, for eligible households living in certain types of buildings or neighborhoods to remain in

---

1. Olsen and Rasmussen, op. cit., p. 9.
2. Olsen and Rasmussen, op. cit., p. 10.

their neighborhood and participate in the program. This, in turn, may compound the difficulties facing lower income neighborhoods as they try to improve the quality of neighborhood housing.

Roles for Neighborhood Groups in the Housing Voucher Program

The efforts of neighborhood groups to improve the viability of their neighborhoods can be enhanced by providing opportunities for non-profit neighborhood based housing organizations to play an active role in the delivery of assisted housing for their neighborhoods. Because these organizations view the provision of assisted housing as a priority concern of their constituencies, relying on neighborhood based organizations increases the likelihood of a long-range commitment to the success of a project. Such a group is likely to continue to attempt to meet the needs of its constituency, to work in maintaining benefits to the neighborhood, and to emphasize the stability and future viability of the neighborhood.

Many neighborhood groups in New York City and throughout the United States have been involved in the delivery of housing services to their neighborhoods, although not always with the direct sanction of the federal government. These activities have included CDBG funded projects, assistance in the administration of housing programs, direct participation in the rehabilitation and management of buildings, and activities to improve the services the services to, and maintenance of, apartments.

As a result of these activities, many neighborhood based housing organizations have developed important skills in providing the following services: packaging of projects, tenant organization, self-help work, rehabilitation, neighborhood improvements, architectural services, management training, energy conservation, cosmetic improvements, housing payments, budgeting, social services and even new construction, among others.

In addition, many neighborhood groups, because they have been working in their neighborhoods for so long, have built up long-time associations and commitments to an area. Regardless of the skills and concerns evident in the administration of public programs, these associations and commitments are luxuries rarely seen in bureaucracies. Assisted housing programs should take advantage of the skills, knowledge and commitments that neighborhood based groups can provide in the delivery of services to their own neighborhoods. Two examples of possible roles for neighborhood groups are provided below.

Representatives of neighborhood groups perceive that households that are eligible for participation in the Section 8 Existing Program sometimes do not participate because they do not always understand what they must do and what they can expect from the program.[1] And, it is too often the case that not speaking English, as always, creates an additional barrier to gaining benefits from the program.

---

[1] As was discussed in Chapter 2, the demand for the Section 8 Existing Program in New York City is far greater than the number of certificates that are available. More than 137,000 households applied for the Section 8 Existing Program in the three year period ending in October, 1981. Between 18,000-21,000 of these households received assistance.

Once a potential recipient decides to apply, successful completion of the process can be exceedingly difficult. Households must be able to fill out forms and be willing to answer questions which may seem personal; they must be able and willing to gather rent receipts and wage statements to prove what may seem obvious; they must be able to assimilate a host of regulations and responsibilities which must be undertaken to benefit from the program, not the least of which may be moving and finding an acceptable apartment within the Fair Market Rent; and then they must wait for an opening to begin looking for a unit if they must move.

The importance of determining income eligibility and the amount of space needed by each household to comply with the quality standards is not questioned. However, the complexity of the program and its reliance on the potential recipient to locate an acceptable quality unit may discourage many certificate holders. Provision of support services to households applying for the programs could minimize these difficulties.

An example of the type of support services that might be offered by neighborhood groups is provided by one of the neighborhood groups in New York City. The group conducts mock procedures that take the prospective Section 8 applicant through all the steps and questions they will be faced with in applying to the City Housing Authority. When they are faced with the actual application process, they have in hand the necessary receipts and papers, they know what questions they will be asked, and they understand how the program will work and what they can expect. The City Housing Authority, of course, has welcomed this assistance from the neighborhood group. The tenants, in turn, are not nearly so frustrated by the procedures and they understand how they can more easily participate in the process.[1]

A second role for neighborhood-based housing organizations is in working with the city to target housing resources to specific neighborhoods. The ability to target Section 8 Existing certificates and housing vouchers to support other funded housing and community development activities is an important mechanism for ensuring that poor residents benefit from these programs and are not displaced.

Primarily through the use of Community Development Block Grant funds, some cities and neighborhood organizations have developed rehabilitation programs and other programs directed to specific neighborhoods or income groups. Ideally, the availability of the vouchers or rent certificates could ensure that lower income households would benefit from these efforts and would not be displaced by the improvements occurring in their neighborhoods.

Cities and neighborhood organizations could guarantee security and support for lower income households that desire to stay in their neighborhoods as rehabilitation and development activities are undertaken within targeted neighborhoods or buildings. Moreover, cities and neighborhood organizations can utilize housing vouchers to achieve selected objectives in neighborhood revitalization efforts, such as economic integration, in-place rehabilitation assistance, or neighborhood stability, by directing a set-aside number of vouchers in tandem with other program activities.

---

[1] Although, the number of Section 8 Existing applicants assisted through October, 1981 (28) is relatively small, the benefits provided the applicants are important.

In New York City, the Housing Authority and the Department of Housing Preservation and Development have set aside 2,853 Section 8 certificates for use in enabling continued occupancy by lower income tenants faced with restructured rents as a result of rehabilitation. These set-aside Section 8 Existing certificates have been used primarily with the Participation Loan Program (PLP), which uses CDBG funds, at 1% interest, to leverage market rate institutional mortgage loans for the rehabilitation of multiple dwellings. The set-aside certificates are also used in conjunction with the Article 8A Loan Program, which provides loans at 3% to private owners of multiple dwellings occupied by low-income tenants. This program is directed to the correction of substandard and/or unsanitary conditions.[1]

In addition, some of these "set-aside" certificates are used by New York City in its attempts to convert its tax-foreclosed occupied housing stock into lower income tenant cooperatives. The Section 8 Existing Housing payments are used to enable tenants in place to pay the economic rents necessary to put these buildings on a self-sufficient footing after they leave public ownership. Although this approach, called "Alternative Management", is in wide use in many marginal or transitional neighborhoods throughout the City and has great potential for achieving some measure of economic integration in rapidly changing neighborhoods, only a very small proportion of the Section 8 Existing certificates are used in conjunction with this program.

One reason for this is that the program has been relatively slow in completing the rehabilitation, restructuring rents and disposing of buildings to tenants or other ownership entities. Nonetheless, the potential exists for an expanded and effective use of rent certificates or housing vouchers in programs such as this.

III. RECOMMENDATIONS REGARDING QUALITY STANDARDS AND THE ROLE OF HOUSING GROUPS

1. Housing units in which recipients of housing vouchers live must be subject to reasonable quality standards.
    a. Except where local standards are insufficient to define or maintain suitable housing, quality standards to ensure the health, safety and livability of housing units occupied through housing vouchers should be locally determined and administered.
    b. Federal standards must be applied where local standards are insufficient to define or maintain suitable housing.
2. Quality standards must be enforced to ensure that housing assistance recipients obtain acceptable housing and that the housing, including the provision of adequate services to occupants, is maintained at the standards. However, in cases where health and safety are not impaired, local units of government should be allowed to administer standards in association with a housing voucher program in such a way that housing choices for "housing poor" households are maximized.

---

[1] City of New York, Department of Planning, "Proposed Seventh Year Community Development Program: Housing Assistance Plan", May 1981, pp. 24-26.

   a. Examples of situations that might require flexibility in administering standards are: need for rent subsidies in neighborhoods where most of the properties do not conform to dominant standards; instances where abandoned or substandard buildings are undergoing tenant, cooperative or other non-profit management and operation for the express purpose of bringing the building up to code; tenant-initiated or non-profit conversions to cooperatives or condominiums; and instances where tenants are using rents to operate the buildings, finance required repairs, or negotiate with the landlord for repairs.

   b. Good faith efforts to meet the standards must be evident for vouchers to be used in each of these situations.

3. Persons otherwise eligible for housing assistance should not be denied assistance for any of the following reasons:

   a. The application of neighborhood quality standards, regardless of the condition of the housing unit.

   b. Discrimination from landlords on the basis of race, sex, size of household or source of income, including the housing voucher.

   c. Private or public action which causes housing units to become unavailable to "housing poor" households.

4. Localities should be encouraged to use all available resources, including production programs, to enable households living in substandard units to receive the voucher without being displaced.

5. The administrative funds allocated to local units of government should not be reduced, since this would threaten the locality's ability to ensure the maintenance of standards in assisted units through annual inspections.

6. Non-profit neighborhood-based housing organizations should have a major role in the delivery of assisted housing to ensure that neighborhood stability is guaranteed. These roles should include: receiving contracts to publicize and market the programs; helping to define the quality standards; locating appropriate housing; and where standard affordable housing is in short supply, developing new and rehabilitated housing.

7. Localities should be given the flexibility to target a percentage of their housing vouchers to preserve and rehabilitate the housing stock and surrounding neighborhoods, provided there are adequate guarantees against displacement.

Glossary of Terms

Population Groups

Eligible Population - all households in New York in 1976 whose gross income was less than or equal to 80% of the New York SMSA median income. The income level used to determine eligibility is adjusted for household size.

Low Income Households - all households in New York City in 1976 whose gross income was greater than 50% and less than 80% of the SMSA median income.

Very Low Income Households - all households in New York City in 1976 whose gross income was less than or equal to 50% of the SMSA median income.

Single Elderly Households - households which contain one adult 62 years of age or older. These households may contain children.

Single Non-Elderly Households - households comprised of one adult less than 62 years of age. These households to not contain children.

One Adult with Children - households which consist of one adult less than 62 years of age and one or more children.

Two Adults with Children - households which consist of two adults less than 62 years of age and one or more children.

Two Elderly Adults - households comprised of two adults, both 62 years of age or older. Children may be present in these households.

Two Non-Elderly Adults - households consisting of two adults both less than 62 years of age. These households do not contain children.

Existing Section 8 Program Participants

Certificate Holders - households certified eligible for the Existing Section 8 Program and issued a certificate authorizing them to search for a unit.

Recipient - households that: (1) have been certified by the Housing Authority as eligible to participate in the program; (2) have an acceptable unit meeting program rent requirements and housing quality standards; and (3) have Section 8 funds paid to their landlords to assist with rent payments.

Non-recipients-households issued certificates authorizing them to search for a unit but who did not locate units meeting program standards. Consequently, these households receive no rent assistance from the program. These households were given a minimum of 60 days, and aften as much as 120 days, to locate a unit meeting program standards.

Movers - among recipients, households that moved to receive the rental assistance, either because they wanted to or because they were required to in order to receive the assistance. Among non-recipients, households for whom a determination was made, based on the condition of the unit they lived in at the time they were issued a certificate, their rent-income ratio, the landlord's willingness to be in the program or their preference, that they had to move to receive assistance.

In-place - among recipients, households that were able to receive the subsidy by remaining in the unit they lived in at the time they were issued a rent certificate. Among non-recipients, households for whom a determination was made, based on their rent/income ratio, that they could receive rent assistance in the unit they lived in at the time they received the certificate, providing the landlord was agreeable and the unit met the quality standards.

Rent Variables

Fair Market Rent - The rent ceiling, set by HUD, for subsidized housing units of specific sizes in the New York SMSA. The fair market rents, which are updated periodically based on changes in local rent levels, include allowances for utilities if they are not included in the unit rent. Certificate holders cannot receive rent assistance if they live in units whose rents exceed the fair market rent for units of corresponding size.

Previous Rent - Gross rent (contract rent plus utilities) paid by recipients immediately prior to enrolling in the program.

Decrease in Tenant Rent Cost - Difference in dollars between the recipients' previous gross rent and their share of the gross rent paid in the Section 8 Program.

Percentage Decrease in Tenant Rent Cost - Percentage change in recipients' actual payments for rent. Computed as follows:

$$\frac{\text{Previous rent - tenant share of gross rent in program}}{\text{previous rent}}$$

Gross Rent in Program Unit - Gross rent for unit occupied by household receiving rent assistance in the Existing Section 8 Program. Sum of the tenant's share of rent and the Public Housing Authority's rent contribution.

Increase of Gross Rent of Unit - Differences in dollars between the gross rent paid by households immediately prior to enrolling in the program and the initial gross rent for the unit in which they received the Section 8 rent assistance.

Percentage Increase in Unit Gross Rent - Percentage difference in the initial gross rent for the unit in which the household received the Sectio 8 assistance and the gross rent paid by the household at their previous address. Computed as follows:

$$\frac{\text{Initial gross rent in Section 8 unit} - \text{Previous gross rent}}{\text{Previous gross rent}}$$

Ratio of Previous Gross Rent to Fair Market Rent - Previous gross rent divided by the fair market rent for a unit of comparable size.

Ratio of Program Gross Rent to Fair Market Rent - Initial gross rent for unit in which Section 8 assistance was received divided by fair market rent for a unit of that size.

Notes on Data and Methodology

The data analyzed were obtained from three sources:

1. 1976 Annual Housing Survey - The Annual Housing Survey, conducted every four years in New York City for HUD by the U.S. Bureau of the Census, interviewed approximately 6,150 households in New York City in 1976.

2. Characteristics of Existing Section 8 Recipients - The New York City Housing Authority records some of the information obtained from recipients at the certification interview and some of the characteristics of the unit rented on a move-in transcript. These data are key-punched and stored on a computer tape. Data for every household which received Existing Section 8 assistance through May 1981 are contained on this tape.

3. Systematic Random Sample of Non-recipients - Basic demographic characteristics and a summary description of why the certificate holder did not use the certificate is maintained for every non-recipient on a 5x7 card in a file cabinet in the Housing Authority. A systematic random sample of 487 non-recipients was drawn. Information was recorded on data collection forms for the 309 non-recipients in the sample issued certificates starting on January 1, 1979. The data collection was restricted to the non-recipients issued certificates on or after 1/1/79 for two reasons. First, it was felt that the experience of households in the most recent past would be most similar or relevant to the situation of households under a housing voucher program. Second, it was important to collect and process the data in as short a period of time as possible.

Since the sample of non-recipients was selected in a scientific manner with a known probability of selection, it was posible to derive estimates of the characteristics of the total population of non-recipients from the sample. These population estimates were combined with the characteristics of the recipients to estimate the percentage of all certificate holders who did not use their certificates.

Background Data

1981 Fair Market Rents for New York City Applicable to the Section 3 Existing Program

Number of Bedrooms	Monthly Rent with Gas and Electric	Utility Allowance
0	$280.	$22.
1	341.	26.
2	407.	32.
3	471.	36.
4	535	40.

1981 Section 8 Income Limits

Number of Persons in Family	Very low Income Limits	Low Income Limits
1	$7,350	$13,950
2	8,400	15,950
3	9,450	17.950
4	10,500	19,950
5	11,350	21,200
6	12,200	22,450
7	13,000	23,700
8 or more	13,850	24,950

Income Standards

# of Persons	Section 8 Very Low Income Per Capita	Low Income Per Capita	BLS Lower Standard	Poverty Level
1	$7,350	$13,950	$ 5,180	$ 4,310
2	4,200	7,975	8,490	5,690
3	3,150	5,983	11,660	7,070
4	2,625	4,988	14,390	8,450
5	2,270	4,240	16,980	9,830
6	2,033	3,742	19,860	11,210
7	1,857	3,386	22,740	
8+	1,731	3,119	25,620	

APPENDIX OF SUPPLEMENTARY TABLES

BLANK PAGE

BLANK PAGE

Table A-1 -- Comparison of New York City and National Very Low Income Population Served by Public Housing and Section 8 Units

	New York City	National
Number of Very Low Income Households	771,047	9,100,000
Percent Served by Section 8 and Public Housing	22.2% (a)	26.4% (b)
Number of Section 8 Units	30,188 (a)	1,700,000(b)
Percent Serving Very Low Income Households	84.1%	82.4%
Number of Public Housing Units	171,585	1,300,000
Percent Serving Very Low Income Households	84.9%	76.9%
Total Percent of Section 8 and Public Housing Units Serving Very Low Income Households	84.8%	80.0%

(a) Includes only Section 8 Existing units.

(b) Includes Section 8 Existing, New Construction, and Substantial Rehabilitation.

Source: New York City Housing Authority Records
Khadduri and Struyk(1980) for national statistics

Table A-2 -- Estimates of Total New York City Population Served by Assisted Housing Programs

Population Category	Number of Households		Very Low Income		Low Income	
	Number	% of Total	Number	% of Total	Number	% of Total
Total Eligible	1,138,802	100.0%	771,041	67.7%	367,761	32.3%
Served by Section 8 Existing	30,188(a)	2.7%	25,375	84.1%	4,813	15.9%
Served by Public Housing	171,585	15.1%	145,676(b)	84.9%	25,909	15.1%
Served by Section 8 New Construction and Subst. Rehab.	45,000(c)	4.0%	na	na	na	na
Total Served	246,773	21.7%	----	----	----	----

(a) Total households on tape = 30,188. Total recipients listed by the Section 8 Existing office = 33,682.

(b) Total includes 149,729 in Federal projects, 21,856 in City and State projects. Only Federal projects provide data on % of households by income categories. Estimates for City and State projects are based on % in Federal projects.

(c) Occupancy breakdowns are not available by income categories for Section 8 new construction or substantial rehabilitation projects.

Table A-3

Percent of Very Low and Low Income Recipient Households by Race

Race	Very Low Income	Low Income
White	58.3%	18.2%
Black	29.9	65.8
Puerto Rican	7.5	10.7
Other Hispanic	3.6	4.5
Oriental	.5	.4
Other	.3	.4
Total	100.0	100.0

Source: New York City Public Housing Authority Records

Table A-4

Percent of Very Low and Low Income Recipient Households by Household Group

Household Group	Very Low Income	Low Income
Single Non-Elderly	14.3%	1.5%
Single Elderly	49.8	8.9
1 Adult w/Children	13.2	51.7
2 Adults w/Children	8.9	24.6
2 Elderly	10.5	7.7
2 Non-Elderly	3.3	5.6
Total	100.0	100.0

Source: New York City Public Housing Authority Records

Table A-5

Percent of Very Low and Low Income Recipient Households by Required Bedroom Size

Required Bedroom Size	Very Low Income	Low Income
0	14.3%	1.2%
1	62.4	22.4
2	16.9	57.8
3	5.6	17.0
4	.7	1.6
5	.05	.02
Total	100.0	100.0

Source: New York City Public Housing Authority Records

Table A-6

Percent of Recipient Households that Moved by Race and Income

Race	Very Low Income	Low Income
White	26.7%	48.6%
Black	48.1	78.9
Puerto Rican	50.3	75.6
Other Hispanic	45.4	73.3
Oriental	38.7	55.6
Other	50.0	83.3
Total	35.6	72.7

Source: New York City Public Housing Authority Records

Table A-7

Racial/Ethnic Composition of Low Income Recipient Households by Household Group

Household Group	Race						
	White	Black	Puerto Rican	Other Hispanic	Oriental	Other	Total
Single Non-Elderly	36.6%	53.5%	9.9%	0.0%	0.0%	0.0%	100.0%
Single Elderly	55.1	39.5	4.0	1.2	.2	0.0	100.0
1 Adult w/Children	6.1	83.9	7.2	2.7	0.0	.1	100.0
2 Adults w/Children	15.7	51.7	20.9	9.8	.8	1.1	100.0
2 Elderly	59.9	27.4	8.1	3.2	1.3	0.0	100.0
2 Non-Elderly	19.1	59.2	13.6	6.3	.7	1.1	100.0
Total	18.2	65.8	10.7	4.5	.4	.4	100.0

Source: New York City Housing Authority Records

Table A-8

Racial/Ethnic Composition of Very Low Income Recipient Households by Household Group

Household Group	Race White	 Black	 Puerto Rican	 Other Hispanic	 Oriental	 Other	 Total
Single Non-Elderly	46.3%	38.4%	11.7%	3.3%	.1%	.2%	100.0%
Single Elderly	69.4	22.5	4.8	2.8	.3	.2	100.0
1 Adult w/Children	17.8	63.4	12.6	5.8	.2	.2	100.0
2 Adults w/Children	54.6	26.7	10.5	5.8	1.4	1.0	100.0
2 Elderly	74.0	15.2	5.5	3.7	1.3	.3	100.0
2 Non-Elderly	63.6	24.1	7.9	3.5	.1	.7	100.0
Total	58.3	29.9	7.5	3.6	.5	.3	100.0

Source: New York City Housing Authority Records

Table A-9

Prevalence of Income Problems Among Household Groups in New York City in 1976

Household Group	Percent of Household Group with Incomes Less than 80% of Area Median	% Very Low Income	% Low Income
Single Non-Elderly	47.9%	65.3%	34.7%
Single Elderly	85.7%	86.8%	13.2%
1 Adult with Children	91.9%	79.1%	20.9%
2 Adults with Children	58.9%	54.0%	46.0%
2 Elderly	62.7%	65.0%	35.0%
2 Non-Elderly	36.4%	54.0%	46.0%
Total Eligible Population	100.0%	67.7%	32.3%

Source: 1976 Annual Housing Survey

Table A-10

Proportion of Racial and Ethnic Groups Among Certificate Holders, Recipients and Non-Recipients 1/79 - 6/81

Household Group	All Households w/Certificates	Recipients	Non-Recipients
White	43.4%	51.9%	28.8%
Black	40.7	35.6	52.1
Puerto Rican	10.8	8.0	14.2
Other Hispanic	4.5	3.8	4.5
Oriental	.4	.5	.3
Other	.2	.3	.0
Total	100%	100%	100%

Source: New York City Public Housing Authority Records

Table A-11

A Comparison of Non-Recipient Households in New York City by Race and Income

Percent of Group

Income Group	White	Black	Puerto Rican	Other Hispanic	Oriental	Total
Low Income	15.5%	61.8%	19.1%	3.6%	0.0%	100%
Very Low Income	34.2%	48.2%	11.6%	5.5%	0.5%	100%
Total	28.8%	52.1%	14.2%	4.5%	0.3%	100%

Source: New York City Public Housing Authority Records

Table A-12

Proportion of Household Groups with Expired Section 8 Existing Certificates in New York City 1/79 - 6/81

Household Group	All Households w/Certificates	Very Low Income w/Certificates	Low Income w/Certificates
Single non-elderly	33.5	33.2	46.6
Single Elderly	[illegible]	28.2	58.6
One adult w/children	44.2	36.6	53.4
Two adults w/children	49.6	32.8	69.6
Two Elderly	16.5	9.8	56.6
Two non-elderly	51.0	39.5	75.0
Overall	36.0	29.5	60.0

Source: New York City Public Housing Authority Records

BEST DOCUMENT AVAILABLE

Table A-13

Comparison of Households Receiving Section 8 Existing Assistance (1976-1981) with Eligible Population (1976) in New York City

Household Group		All Eligible Households		Very Low Income Households		Low Income Households	
		Popln.	Sec. 8 Tenants	Popln.	Sec. 8 Tenants	Popln.	Sec. 8 Tenants
Single non-elderly		16.9	12.3	16.3	14.3	18.1	1.5
Single elderly		19.3	43.2	24.7	49.8	7.9	8.9
One adult w/children		16.7	19.4	19.5	13.2	10.8	51.7
Two adults w/children		22.4	11.4	17.8	8.9	31.8	24.6
Two elderly		11.7	10.0	11.2	10.5	12.6	7.7
Two non-elderly		13.2	3.7	10.5	3.3	18.8	5.7
Total	#	1,138,802	30,188	771,041	25,375	367,761	4,813
	%	100%	100%	100%	100%	100%	100%

Source: New York City Public Housing Authority records and the 1976 Annual Housing Survey.

Table A-14

Summary Data for New York City's Section 8 Existing Program 1976 - 1981

Approximate number of certificates issued 6/1976 - 6/81	50,748
Approximate number of households assisted	33,682
Approximate number of expired certificates	13,682

Program History Since 1/1/79 by Income Level

	Very Low Income	Low Income	Total
Households issued certificates	78.6%	21.4%	23,173 (100%)
Households assisted	86.7%	13.3%	14,830 (100%)
Households with expired certificates	64.4%	35.6%	8,343 (100%)
1976 Eligible population	67.7%	32.3%	(100%)

Source: New York City Public Housing Authority Records

Table A-15

	Percent Movers		Certificate Holders	
Household Group	Recipients	Non-Recipients	Percent of Movers that are Non-Recipients	Percent of In-Place that are Non-Recipients
Single Non-Elderly	46.7%	74.4%	44.6%	19.5%
Single Elderly	27.9	64.6	50.8	16.4
One Adult w/Children	55.1	90.2	56.5	14.7
Two Adults w/Children	54.3	90.6	62.2	16.9
Two Elderly	27.8	92.9	43.4	2.2
Two Non-Elderly	38.4	85.7	69.9	19.5
Overall	38.6	80.6	54.0	15.1

Source: New York City Public Housing Authority Records.

Table A-16

Reason Listed by Housing Authority Staff for Expiration of Section 8 Certificate, 1979 - 1981

	Status of Household	
Reason Coded by Housing Authority	Move	In-Place
Tenant could not find apartment in preferred location.	6.8	0
Landlord not willing to rent to tenant.	4.[illegible]	50.0
Apartments located did not meet rent, rent hardship, size or quality standards.	5.4	16.7
Household voluntarily dropped out.	17.7	16.7
Household could not find unit in specific neighborhood listed by Housing Authority.	24.9	10.0
Tenant unable to rent referrals offered.	38.2	1.6
Change in family eligibility status.	2.0	5.0
Total	100.0	100.0

Source: New York City Housing Authority files on expired certificates.

PARTICIPATING ADVISORY PANEL MEMBERS*

Jose Acuna, Executive Director
Manhattan Valley Corporation

Margie Allen, Associate Director of Community Development
New York State Urban Development Corporation

Candy Bayer, Executive Director
Task Force on City-Owned Property

Richard Berman, Executive Director
New York State Division of Housing and Community Renewal

[illegible] Bhatnagar, Director of the Housing Division
New York City Planning Commission

Charles Brass, Representing Program and Management Analysis
Housing Preservation and Development

Bonnie Brower, Director
Association of Neighborhood Housing Developers

Howard Burchman, Director
Howard Burchman and Associates

Nancy Castleman
Fund for the City of New York

Cushing Dolbeare, President
National Low Income Housing Coalition

Richard Duhan, Regional Director
New York State Office of Urban Revitalization

Roberta Edge, Representing Program and Management Analysis
Housing Preservation and Development

Barbara Gordon Espejo, Esq., Attorney
Mudge, Rose, Guthrie and Alexander

Jack Freund, Representing Program and Management Analysis
Housing Preservation and Development

Anthony Gliedman, Commissioner
Housing Preservation and Development

Bruce Gould, Executive Director of Program and Management Analysis
Housing Preservation and Development

Congressman William S. Green
New York State Congress

Kim Hamilton, Deputy Director of Program and Management Analysis
Housing Preservation and Development

---

*Titles for Affiliation Only

William Hill, General Manager
Bush Terminal Association

Kent Hiteshew, Mayor's Office of
Intergovernmental Relations

David Hunter, Executive Director
Stern Fund

Cynthia Jachles, Legislative Analyst
New York City Office of Management and Budget

Adina Johnson, Acting Executive Director
Operation Open City

Marcie Kesner, Special Assistant to the City Council President

Galen Kirkland, Representing West Harlem Community Organization

Charles Laven, Private Consultant
Urban Homesteading Assistance Board

Frances Levenson, Vice President
New York Bank for Savings

Joseph McMahon, Private Consultant
McMahon and Associates

Margaret McNeill, Director
West Harlem Community Organization

Joseph McNeely, Consultant
Public-Private Partnerships

Very Rev. James P. Morton, Dean
St. John the Divine Cathedral

Andrew Mott, Executive Director
Center for Community Change

Karen Murphy, Assistant Project Development Coordinator
Housing Preservation and Development

Anita Nager, Funds Administrator
Fund for the City of New York

Roberto Nazario, Consultant
Community Information Services

Meyer Parodnick, President
Consumer Farmer Foundation, Inc.

Daniel Persons, District Council #37

Tom Robbins, Editor, *City Limits*

Susan Seifert, Representing Program and Management Analysis
Housing Preservation and Development

James Sleeper, Consultant

Lorie Slutsky, Program Officer
New York Community Trust

Michael Stegman, Professor of Urban Planning
University of North Carolina

Herbert Sturz, Chairman
New York City Planning Commission

Betty Terrell, Former Executive Director
Association of Neighborhood Housing Developers

Juan Villanueva, Vice President
Chemical Bank

Martin Young, Assistant Secretary
Consumer Farmer Foundation

Barry Zigas, Director of Legal Action
U.S. Conference of Mayors

Harry DiRienzo, Consumer Farmer Foundation
formerly of Banana Kelly

Sidell Knepper, Representing Commissioner Berman
New York State Division of Housing and Community Renewal

BEST DOCUMENT AVAILABLE

HOUSING ROUNDTABLE*

Jose Acuna, Executive Director
Manhattan Valley

Jess Ambers, Director
Prospect Lefferts Gardens Neighborhood

Sandy Bayer, Director
Task Force on City-Owned Property

Bob Blank, Director
Flatbush Development Corporation

Bonnie Brower, Director
Association of Neighborhood Housing Developers

Maurice Callendar, Executive Director
West Harlem Group Assistants

Logy Cedina
Renigades Housing Movement

Harriet Cohen
Neighborhood Anti-Arson Center

Roi Crouch, Director
Pratt Area Community Council

Harry DiRienzo, Consumer Farmer Foundation, formerly of Banana Kelly

Gary Sam Hattem, Executive Director
St. Nicholas Neighborhood Preservation and Housing Rehabilitation Corp.

Adina Johnson, Acting Executive Director
Operation Open City

Rabbi Shmuel Lefkowitz
Southern Brooklyn Community Organization

Margaret McNeill, Executive Director
West Harlem Community Organization

Carlos Martinez
Renigades Housing Movement

Doug Moritz
Los Sures

John Nettleton, Community Service Society

Meyor Parodnick, Consumer Farmer Foundation

Fred Ringler, Representing People's Firehouse

Yvette Shiffman, Community Service Society

Sondra Thomas
Clinton Housing Development Corporation

Ron Webster, Director
People's Firehouse

Renee Williams
Erasmus Neighborhood Federation

---

*Titles for Affiliation Only

Chairman **Gonzalez**. Thank you very much, Mr. Shiffman, for a very important and impressive presentation. We are grateful to you

There is just one thing that I have noticed. On page 6, the last paragraph, you say, "We oppose the congressional limitation on eligibility to 50 percent of the median income." That is not congressional.

Mr. **Shiffman**. Well, Congress passed it last year. It was an act of Congress limiting it to 50 percent of the median income. It is an administrative proposal to continue that, but it was a congressional action last year. It probably came from the Senate side.

Chairman **Gonzalez**. Well, of course, I think this came after we got into the reconciliation, if I remember correctly, but I don't think I am incorrect in the impression I had when I read this that the Congress did not actually mandate the 50 percent. It still referred to 80 percent but said it may come in and compromise between 50 and 80 percent.

Am I not correct on that?

Mr. **Shiffman**. I stand corrected.

Chairman **Gonzalez**. It just caught me because that was a big thorn in my side all during that painful reconciliation process last year.

Well, without any further ado, I am going to recognize Mr. Schumer. I should have given him a chance to introduce you because I know you have worked very closely together.

Mr. **Schumer**. Thank you, Mr. Chairman.

We have heard a lot of testimony, but this is truly a superb job. I mean I just think it is excellent. It will be extremely helpful to me in modifying my particular part of the legislation. Some of your suggestions I know you are making in a normative, ideal world sense, and in an ideal world I would make them too, but some of them I think we can add to our bill with very little political damage.

As you know, we are trying to build a coalition of people who don't often think the way you and I and the chairman do, and we do have to reach out.

What we have done with the 20-percent set-aside is to make it a minimum. Localities that apply can go higher, and one of the things we will consider writing in is some kind of priority for projects which contain a higher percentage of low income.

I am a little hesitant to mandate more than 20 percent. We are having a rough enough time getting developers, those who we hope to help us persuade our counterparts in the Senate, and some of our more conservative colleagues in the House to go along even with the 20 percent. The same is true for the 15 years. We are considering establishing a priority for projects which have a longer commitment. But maybe we can find a way to mandate it further.

I really don't have any questions. I think you have done an outstanding job and one that is going to be very helpful to me in crafting changes to the bill. Of all the testimony we have heard, this is like food: it is good to eat, it is good to digest. So thank you, Ron.

Mr. Chairman, Ron Shiffman is one of the outstanding forces in New York City. You know, we have our own versions of Reaganomics in New York City, and he has been a steadfast fighter against those. Maybe one day his vision for our city and for our country will succeed and the country will be a lot better off.

Chairman **Gonzalez**. I did not realize that you had a New York version of Reaganomics. I thought the big issue there was Koch-22.

Mr. **Schumer**. That is the version.

Chairman **Gonzalez**. Thank you for that because the record ought to show it. We have had before some exposure from this subcommittee for Mr. Shiffman, I believe. Didn't we have some material or presentation last year?

Mr. **Shiffman**. I believe so, yes.

Chairman **Gonzalez**. And we are very grateful. I sincerely say that because in my opinion, you know, you hit on target, and it is very important to the process of these hearings to have your testimony, and I repeat, we are very grateful for your time.

Mr. **Schumer**. One other thing, if I might, Mr. Chairman.

One of the areas in the package where we really want to succeed is in keeping public housing operating subsidies at an adequate level. I know you did not mention operating subsidies specifically although you did talk about public housing as a form of new construction. As you may know, last year, due to the chairman's efforts we succeeded in getting not only the other side of the aisle but the other Chamber to agree to authorize more money for public housing subsidies than either Carter or Reagan had proposed. This was perhaps the only program where we met success, and we are going to make a strong effort to do that again.

I just feel that even the most conservative member of our committee can understand that to conserve the $65 billion investment we have in public housing, we are going to have to increase operating subsidies. I know you feel that way, but you probably just thought we would all agree.

Mr. **Shiffman**. If I may just say, I would also like the record to show that Frank DeGiovanni, who is with me today, really played a major role in both the testimony and in the development of the housing voucher study.

Chairman **Gonzalez**. I also wanted to comment on the fact that what you said with reference to the voucher program was very, very good. I think you presented one aspect there, and I said this last year when I met with the chairman and vice chairlady and executive secretary when they said it would have to be limited because it would not be an entitlement program at all, and at that point, you know, I realized that it was not going to meet the problem that we are confronting at this moment, and what you had to say was very, very good. I want to compliment you on that.

Mr. **Shiffman**. Thank you again. Thank you for having me.

Chairman **Gonzalez**. Thank you again very much.

The subcommittee stands in recess until tomorrow morning at 9:30, again in this room, 2128.

[Whereupon, at 6 p.m., the hearing was recessed, to reconvene at 9:30 a.m. the following day, Wednesday, March 24, 1982.]

[The following additional correspondence was received for inclusion in the record:]

HOUSING AUTHORITY
P.O. BOX [illegible]
EL PASO, TEXAS [illegible]

[illegible] MONTANA
915 [illegible]

EL PASO

MARCH 22, 1982

HOUSE SUBCOMMITTEE ON HOUSING AND
COMMUNITY DEVELOPMENT
RAYBURN HOB - #2252
WASHINGTON, D. C. 20515

ATTENTION: GAIL JO BEAGLE

DEAR MS. BEAGLE:

THANK YOU FOR THE INFORMATION PERTAINING TO H.B. 5731; WE HAVE IT UNDER STAFF REVIEW FOR COMMENT.

I AM ENCLOSING WRITTEN TESTIMONY FOR EACH MEMBER FOR INCLUSION IN YOUR HEARINGS. HOPEFULLY, A COMPROMISE CAN BE WORKED OUT WITH THE ADMINISTRATION.

WE WOULD APPRECIATE ANY ASSISTANCE IN HAVING HUD COMMIT ITS FFY 1982 FUNDS, AS THE EPHA HAS A NINE (9) MILLION DOLLAR REQUEST FOR RENOVATION OF THREE (3) COMPLEXES AT HUD/DALLAS AREA OFFICE.

THANK YOU FOR YOUR CONSIDERATION AND COOPERATION.

SINCERELY,

SALVADOR F. CANCHOLA, PHM
EXECUTIVE DIRECTOR

SFC/LA
ENCLS.

MARCH 19, 1982

WRITTEN STATEMENT OF SALVADOR F. [illegible], [illegible]
[illegible] DIRECTOR, HOUSING AUTHORITY OF THE CITY OF EL PASO, TEXAS
[illegible] AND APRIL [illegible], 1980, AND FORMER EXECUTIVE DIRECTOR, BROWNSVILLE,
[illegible] HOUSING AUTHORITY, JULY 1, 1976, TO MARCH [illegible], 1980

[illegible] SUBMITTED TO THE [illegible] SUBCOMMITTEE ON HOUSING AND COMMUNITY DEVELOPMENT
[illegible] ON BANKING, FINANCE AND URBAN AFFAIRS AND THE COMMITTEE ON THE BUDGET.

[illegible] THE [illegible] IN [illegible] HOUSING AND HUD RELATED PROGRAMS [illegible] INFLATION, SOCIAL PROGRAMS AND WELFARE RUNNING [illegible] THE [illegible] WITH A [illegible] APPROACH FOR PROBLEM SOLVING COMBINED WITH [illegible] APPROACH TO LEGISLATION. WELFARE AND SOCIAL CHANGE CONCEPTS, [illegible] OF TRYING TO BE ALL THINGS TO ALL PEOPLE AT ALL TIMES, AS [illegible] NEW YORK CITY, [illegible] LED TO THE PASSAGE, IN 1969, OF THE BROOKE AMENDMENT WHICH LIMITED THE RENTS CHARGEABLE TO RESIDENTS IN HUD-ASSISTED PROGRAMS; [illegible] IMPORTANT, WAS THE SALIENT EFFECT OF ELIMINATING MINIMUM RENTS, WHICH, IN [illegible] OF THE UNIT MANAGER. THIS CREATED THE "ZERO" AND "NEGATIVE" [illegible] FOR WELFARE RECIPIENTS, OR THOSE LARGER FAMILIES WITH LITTLE INCOME. THE [illegible] FUTURE AND FISCAL STABILITY FOR PUBLIC HOUSING AUTHORITIES [illegible] AS THE FINANCIAL FLOOR WAS REMOVED. WHATEVER LEGISLATION IS ADOPTED IN [illegible], EITHER THROUGH A NEW HOUSING ACT, APPROPRIATION OR BUDGET, I WOULD RECOMMEND FIRST AND FOREMOST THAT A MINIMUM RENT BE ESTABLISHED OF AT LEAST SIXTY DOLLARS ($60.00) MONTHLY EFFECTIVE JANUARY 1, 1983. FURTHER, THAT MINIMUM RENTS BE ADJUSTED ON A NATIONWIDE BASIS USING THE ECONOMIC FACTORS

CURRENTLY USED TO COMPUTE FAIR MARKET RENTS OR INCOME LIMITS. BY USING THE NATIONAL LEASED HOUSING ASSOCIATION'S FEASIBILITY STUDY FOR "30% OF INCOME FOR FAMILIES THAT EARN 80% OF MEDIAN INCOME FOR SELECTED CITIES", THE FOLLOWING PERCENTAGE VARIANCE FROM A NATIONAL AVERAGE HAS BEEN CALCULATED:

EAST	%	MIDWEST	%	SOUTH	%	WEST	%
BOSTON	+19	COLUMBUS	+ 2	BIRMINGHAM	-13	LOS ANGELES	+12
NEWARK	+54	INDIANAPOLIS	+ 6	NASHVILLE	- 6	SALT LAKE CITY	+ 5
PITTSBURGH	+ 6	MADISON	+11	SAN ANTONIO	-15	SEATTLE	+28
PROVIDENCE	+ 2	MINNEAPOLIS	+17				

THE MINIMUM RENT FLOOR UNDER HUD SUBSIDIZED PROGRAMS WOULD NOT INSURE FINANCIAL STABILITY, BETTER MANAGEMENT, OR IMPROVED LIVING CONDITIONS BUT PRESSURE WOULD BE TAKEN OFF THE WORKING POOR WHO SUPPORT AND CARRY THE LOAD FOR ASSISTED HOUSING.

2. ASSISTED HOUSING IS CAUGHT IN A TUG-OF-WAR BETWEEN THE ADMINISTRATION WHICH WANTS TO ELIMINATE ALL LONG-TERM COMMITMENTS (PUBLIC HOUSING, SECTION 8/NEW CONSTRUCTION, ETC.), AND A CONGRESS WHO STILL ADHERES TO THE PRECEPTS UNDER THE GREAT SOCIETY. UNFORTUNATELY, LEGISLATORS MUST ESTABLISH POLICY FOR FIFTY (50) STATES THAT DOES NOT ALLOW ENOUGH FLEXIBILITY FOR LOCAL CONDITIONS WHICH VARY FROM HOUSTON, WHERE EVERYTHING IS BOOMING; TO DETROIT, AN AREA ON THE ROPES; TO MIAMI, A CITY SUFFERING FROM CRIME AND IMMIGRATION; TO EL PASO, SUFFERING FROM A POOR ECONOMY ALONG THE MEXICAN BORDER. THEREFORE, MY SECOND RECOMMENDATION IS FOR A BLOCK GRANT ALLOCATION FOR ASSISTED HOUSING PROGRAMS TO INCLUDE THE CURRENT FUNDING MECHANISMS IN EXISTENCE (I.E., LOW RENT HOUSING, HAPP/EXISTING, NEW CONSTRUCTION, MODERATE REHABILITATION, SUBSIDY, MODERNIZATION, ETC.), PLUS ANY NEW PRODUCTION PROGRAMS. THE PRECEPT OF REAGANOMICS IS "RETURNING CHOICE TO

BEST DOCUMENT AVAILABLE

THE STATES AND CITIES", BUT WITH THE ADMINISTRATION'S ATTITUDE OF RECISSION OF CURRENT COMMITMENTS AND ONLY THE NEW MODIFIED VOUCHER SYSTEM BEING FUNDED ARE ALL TOO REALISTIC THROWBACKS TO THE 1973 NIXON MORATORIUM AND 1975 HUD POSITION OF SECTION 8 BEING THE "ONLY GAME IN TOWN."

3. THE RECISSION OF THE DAVIS-BACON WAGE RATE SCHEDULE FOR HUD-ASSISTED HOUSING WOULD NOT ONLY LOWER CONSTRUCTION COSTS, BUT MAKE WORK MORE COMPETITIVE. NATURALLY, SUCH A MOVE WOULD BE VIGOROUSLY OPPOSED IN UNION ORIENTED AREAS, BUT THE EDGE IN PRODUCTION AND EMPLOYMENT MUST CERTAINLY BE REGAINED TO MAKE CONSTRUCTION A VIABLE TOOL TO REDUCE UNEMPLOYMENT.

4. THE DEMOLITION OF 5,000 UNITS OF HOUSING, AS PROPOSED BY THE ADMINISTRATION, COULD BE ACCOMPLISHED READILY BY RETURNING PUBLIC HOUSING COMPLEXES WITH PAID UP ANNUAL CONTRIBUTION CONTRACTS TO THE CONTROL AND OWNERSHIP OF THE HOUSING AUTHORITY INSTEAD OF RETAINING THEM UNDER HUD'S CONTROL WITH NEW ACC'S THAT WERE PREDICATED ON SUBSIDY FUNDS. A CASE IN POINT BEING TEX 7-1, BUENA VIDA, 150 UNITS, TEX 7-2, BOUGAINVILLEA, 49 UNITS, AND TEX 7-3, VICTORIA GARDENS, 46 UNITS, IN BROWNSVILLE, TEXAS, WHICH HAD PAID ACC'S IN MARCH, 1981, BUT REMAIN UNDER ACC ALTHOUGH THEIR INCOME IS $110.00 PER UNIT MONTHLY AND EXPENSES ARE $97.00. HUD RETAINED CONTROL OF THESE COMPLEXES, WHICH EQUAL 5% OF THE ADMINISTRATION'S TARGET LIST FOR DEMOLITION TO PREVENT LOSS OF UNITS AND NEED FOR MANAGEMENT REVIEW PERSONNEL. NATURALLY, THERE ARE MANY PAID OUT COMPLEXES WHICH ARE FACING ECONOMIC CALAMITY AND PHYSICAL DESTRUCTION. THESE UNITS SHOULD BE RETURNED TO THE LOCAL GOVERNMENT FOR DEMOLITION, SALE OR SOME TYPE OF URBAN HOMESTEADING, BUT ON A CASE-BY-CASE BASIS.

5. THE UNTIMELY DELAY IN ALLOCATION OF FUNDS BY THE ADMINISTRATION AND HUD CAUSES A BACKUP OF PROGRAMS AND WORK PERFORMANCE WITH HURRY-UP-AND-WAIT BEING

THE RESULTANT ATTITUDE. TOWARD THE END OF THE FEDERAL FISCAL YEAR, FUNDS ARE DISBURSED WITH AN EXTREMELY SHORT TIME FRAME, WITH POOR PERFORMANCE AND SLOPPY ALLOCATION BECOMING A SELF-FULFILLING PROPHECY. I RECOMMEND DISBURSEMENT OF FUNDS ON A TIMELY BASIS, AND PUBLISHING OF ALLOCATIONS, REGULATIONS, ECONOMIC FACTORS, ETC., NOT LATER THAN OCTOBER 1 FOR THE ENSUING FEDERAL FISCAL YEAR. HUD'S ATTITUDE OF PRODUCTION ON A SLOW TRACK BASIS AND REWARD OF NON-PERFORMANCE SHOULD BE ELIMINATED, BOTH INTERNALLY AND IN DEALING WITH OUTSIDE AGENCIES.

6. THE INSTALLATION OF UTILITY CHECKMETERS, WHERE FEASIBLE, WILL REDUCE GLUTTONOUS CONSUMPTION AND INSTILL IN RESIDENTS A DESIRE FOR CONSERVATION. UNDER THE PERFORMANCE FUNDING SUSBIDY (PFS) FACTORS FOR ASSISTED HOUSING, UTILITIES WERE A FULLY REIMBURSABLE ITEM.

MR. CHAIRMAN, I WILL GLADLY PRESENT ADDITIONAL INFORMATION IN PERSON OR WRITTEN UPON THE COMMITTEE'S REQUEST. IN CLOSING, HOUSING AUTHORITIES ARE NO DIFFERENT THAN FAMILIES, BUSINESSES OR INDUSTRIES AND MUST INCREASE THEIR INCOME TO OFFSET EXPENSES, OR FACE FORECLOSURE AND BANKRUPTCY.

#####

EQUAL HOUSING
OPPORTUNITY

HOUSING AUTHORITY OF GLOUCESTER COUNTY

COLONIAL PARK APARTMENTS
401 S. EVERGREEN AVENUE
WOODBURY, NEW JERSEY 08096

(609) 845-4959

FRANK B. SMITH
CHAIRMAN
WILLIAM F. SHARP
VICE CHAIRMAN
WAYNE H. TRIPLETT
SECRETARY
JOSEPH A. REED
TREASURER
RICHARD E. PHILBIN
COMMISSIONER
ALPHONSO L. SMITH, M.D. PhD.
COMMISSIONER
RUSSELL C. NAYLOR
COMMISSIONER

FRANK C. COSSABOON
EXECUTIVE DIRECTOR

March 24, 1982

The Honorable Henry B. Gonzalez
Member of Congress
Chairman, Subcommittee on Housing and
Community Development
2252 Rayburn House Office Building
Washington, D.C. 20510

RE: Special Report on Section 8 Moderate Rehabilitation
Housing Program
Gloucester County New Jersey Housing Authority

Dear Congressman Gonzalez:

The Section 8 Moderate Rehabilitation Program is a unique program which simultaniously meets several objectives. First, the program provides standard rental housing for low to moderate income tenants with the recipients paying a reasonable portion of their income 25%, towards the cost of their housing. Secondly, the program revitalizes neighborhoods by acting as a catalyst to encourage other owners to improve their property. Thirdly, the program upgrades individual units making them viable tax producing dwellings within their respective communities. Fourth, the program prevents the spread of housing deterioration.

The Housing Authority of Gloucester County in New Jersey has successfully administered this complex but workable program. To date 95 rental units have been rehabilitated. The work which has been completed has made significant improvements in the housing stock. Included under the scope of work undertaken are the following improvements:

> Plumbing improvements, electrical improvements, new and upgraded heating systems, re-roofing, structural repairs, siding installation, insulation and weatherization, window repair and replacement, storm windows and new doors and new or improved kitchens and baths.

The financing for these units has principally originated from private financial institutions. The total amount of capital utilized for rehabilitation and refinancing has exceeded 1.2 million dollars. Included in ths figure are community development funds and owner investment. Community Development Programs have contributed approximately $38,000 in grants and the property owners have invested approximately $77,000 in personal funds. Well over sixty percent of the remaining 1.1 million dollars raised through the private banking system has been used for rehabilitation. This figure amounts to $687,000 which averages out to approximately $7,200 per unit. The remaining $413,000 has been used to refinance poorly structured debt.

All rehabilitated units under Housing Assistance Payments Contracts are occupied. The average monthly cost to the Housing Authority through rental subsidies is $240.00 per unit per month. We feel this is a very low cost for providing assisted housing in comparison to new construction or substantial rehabilitation.

This office is constantly surveying the local housing stock through the Section 8 Existing Program and the Moderate Rehabilitation Program. There is very obviously a need for upgrading rental units which otherwise will remain in disrepair, under utilized, be non-tax producing and a blighting influence in their communities. It is very clear through our detailed financial analysis of the units submitted to the Authority that upgrading would not occur without the Moderate Rehabilitation Program. For rehabilitation to take place the owner's total costs must be covered under the rents which seldomly can occur in today's market given the current interest rates and the cost of rehabilitation.

It is the position of this office that the Moderate Rehabilitation Program is a viable, cost effective program which should not be under funded or discontinued.

We are willing to provide more specific information, photographs and other data or personally relate our experiences in housing rehabilitation through the Moderate Rehabilitation Program if you so desire.

Please feel free to contact me.

Very truly yours,

Frank C. Cossaboon

Frank C. Cossaboon
Executive Director

Virgin Islands Housing Authority
Post Office Box [illegible] 7668
Charlotte Amalie
St. Thomas, U.S. Virgin Islands 00801

Telephone 809 774-2741

Office of Executive Director

March 4, 1982

Gerald R. McMurray
Staff Director
Subcommittee - Housing & Community Development
Committee on Banking, Currency and Housing
U.S. House of Representatives
2129 Rayburn Building
Washington, D.C. 20515

Dear Mr. McMurray:

I would like to take this opportunity on behalf of the Board of Commissioners and myself to express our sincere appreciation for taking the time to meet with us on February 1, 1982 to discuss matters of vital concern regarding the Virgin Islands Housing Authority.

The meetings with you and other HUD Officials, both in Washington, D.C. and New York, proved productive and our Position Paper was well received.

We are pleased that you are considering placing the VIHA Position Paper in the Legislative Record and we are willing to testify or provide any additional information that you may require.

Again thank you for extending to us the opportunity to discuss our mutual concerns. In the near future I will be forwarding copies of our latest Annual Report and "Housing At A Glance," an informative handbook on the housing communities owned and operated by the Virgin Islands Housing Authority.

Thank you for your interest and cooperation.

Sincerely,

Floyd Williams

Floyd Williams
Executive Director

FW/cas

encl: VIHA Position Paper

VIRGIN ISLANDS HOUSING AUTHORITY

POSITION PAPER

The Virgin Islands Housing Authority provides more housing per capita than any other PHA in the Nation. Approximately 21% of the Territorial population reside in housing communities operated by this Authority.

Proposed decreasing reliance of Federal financial support, coupled with the unique problems here in the Virgin Islands hinder the Authority in carrying out its major objectives of operating on a sound efficient basis while providing adequate services to tenants.

This paper will look at the Virgin Islands Public Housing Program as it exists today and try to bring into focus some of the major issues confronting the PHA.

Background

The Virgin Islands Housing Authority (VIHA) is a public housing corporation that operates under the provisions of the U.S. Housing Act of 1937, as amended, and the Virgin Islands Code. The birth of the VIHA dates as far back as 1941 when the municipal councils of both St. Thomas/St. John and St. Croix passed an ordinance creating municipal housing authorities for each island. Bill No. 5, passed by the Virgin Islands Legislature in 1949, incorporated the municipal housing authorities into a single agency (VIHA) with tri-island jurisdiction. In 1962, Act No. 903 of the Virgin Islands Legislature provided for an amiable judicial separation, with the Virgin Islands Housing Authority once again acknowledged by its given name of 1941.

The Housing Authority is governed by a Board of Commissioners consisting of seven (7) members who are appointed by the Governor of the Virgin Islands and confirmed by the Legislature for three (3) terms and so staggered that the terms of two commissioners expire on January 1st of each year. In accordance with Title 29, Section 32 of the V.I. Code, two (2) of the Commissioners shall be tenants of public rental housing projects, one (1) of which tenant shall be a resident of St. Croix, and the other of which shall be a resident of St. Thomas.

Pursuant to the V.I. Code, Title 29, Section 33, the Commissioner of the Department of Housing and Community Renewal serves as Chairman of the Board of Commissioners of the Virgin Islands Housing Authority. Regular Board meetings are scheduled for the third Wednesday in each month. Special Board meetings are held as required throughout the year. All Board meetings are usually held at the VIHA Central Office at Estate Anna's Retreat in St. Thomas, and at the John F. Kennedy Terrace in Christiansted, St. Croix, and are open to the public.

The VIHA is empowered with the responsibility for planning, financing, constructing, maintaining, and managing public housing developments on the islands of St. Thomas, St. John and St. Croix, to include 5,176 units and comprising approximately 15% of the total territorial housing stock. By virtue of its ownership in these properties, the VIHA is the largest "Landlord" in all the islands and by necessity, must perform all the functions of a private owner (rent collection, leasing of units, and maintenace), in addition to providing an increasing variety of social services to the 20,295 residents of low-rent public housing developments, approximately 21% of the total territorial population.

* * * * *

The following are the issues which will be addressed:

1. The Performance Funding System (PFS)

The Performance Funding System provides the current formula for determining a PHA's rate of subsidy and is the basic tool for attempting to make up the difference between the amount of rent a resident pays for a unit and the cost to the Authority for operating it.

The Virgin Islands Housing Authority is excluded from the Performance Funding System by Congressional action. The Management Review conducted in April 1980 by officials from the Area, Regional and HUD Central Office clearly conceded that the Virgin Islands Housing Authority's exclusion from the non-PFS formula adversely affects our operations.

Utilities and other costs beyond the control of the Authority contributable to unique circumstances may be considered for supplemental operating subsidy funding according to FR 7475.13, Section 890.108(d). The Regional Administrator's letter of February 13, 1981 states that HUD has developed a revised formula which will include uncontrollable costs. Recent conversations with Regional representatives have indicated that the new formula has not been finalized.

The VIHA has scheduled a meeting with the Area HUD Office in Hato Rey, Puerto Rico, to discuss the requisitioning of funds. We are desirous of obtaining the formula currently being used to determine our operating subsidy and the amount of operating funds that will be made available to us for 1982.

For Fiscal Year 1981, the VIHA requested an operating subsidy of $5,747,260 and received operating subsidy of $2,968,828. The Authority is requesting an increase to $5,096,370 for 1982. These subsidies are urgently needed to maintain the fiscal viability of the Authority. If HUD follows the same pattern of funding as for 1981, we can expect an increase of 10% in operating subsidy. We feel that in order to become more efficient, our budget should reflect our actual needs; however, if we are unable to obtain adequate subsidy, cutbacks would be implemented as necessary.

We are aware that the stringent fiscal restraints generated by President Reagan's Economic Policies may not allow a subsidy in excess of 10% for 1982; however, consideration must be given to a more realistic inflation rate in the Virgin Islands, which according to the HUD Area Office Economist is between 18-20%. For this reason, this Authority contends that the application of a national operating subsidy rate of 9.88%, as utilized in granting 1981 subsidies is inequitable.

2. Utility Costs

The Virgin Islands Housing Authority provides water at no charge to the residents. Residents pay for electricity and gas. This utility allowance is deducted from gross rent. This utility schedule is the primary reason for negative rents wherein the Authority is obligated to reimburse the residents.

The PFS Section 890.110(c) addresses "severe financial crisis" from utility rate increase wherein the Authority furnishes all utilities. There is no consideration given to the loss of income due to utility rate increase which results in contract rents of zero or negative rents. The estimated dwelling rental loss of $737,880 projected for 1982 clearly warrants some special consideration from HUD. The financial crisis resulting from the forthcoming revised utility schedule is as much a cost beyond the Authority's control as the financial crisis resulting from a utility rate increase wherein the Authority paid for the utilities.

a. Water

For Fiscal Year 1982, the Authority is requesting $1,611,051 from HUD to purchase water. Water is purchased by VIHA from the following sources:

	Cost Per Ton	Cost Per Thousand Gallons
Government of the V.I.	$ 2.13	$ 8.50
Donoe Water Services	1.35	5.40
S.E. Harthman	1.50	6.00
Aquarian Systems, Inc.	1.50	6.00
Demco, Inc.	3.50	14.00

The water expenditures for 1981 approached $1,239,300. Since the Government of the Virgin Islands has just increased the price of water from $6.50 to $8.50 per thousand gallons, we anticipate a similar 30% increase. A further increase in the price of water during 1982 is also expected later in the year.

Another vital factor that increases the cost of water expenditures has been the recent elimination of water rationing which has drastically increased the quantity of water now being consumed by VIHA's resident population. The residents could not use what was not there to use. However, with the full availability of water, usage has increased dramatically.

b. Electricity

For 1982, the Authority projects electricity expenditures of $372,000 which is a nine percent (9%) increase over the 1981 expected expenditures of $342,000. The prime reason for the continual increase in this expense is the fuel escalator adjustment used in billing.

The rate changed by the V.I. Water and Power Authority varies depending on the fuel escalator adjustment. The fuel escalator adjustment is added to each bill depending on what the Water and Power Authority pays for the oil to make the electricity. Water and Power Authority has been having problems with its more efficient plants and has been forced to use the less efficient but more fuel consuming plants. This most naturally results in a higher fuel escalator adjustment.

The January 1982 charges for electricity are as follows:

Customer Charge Per Month

Residential		Commercial	
Single Phase -	$ 2.73	Single Phase -	$ 2.68
Three Phase -	7.45	Three Phase -	9.71
First 200 KWH -	0.0900 P/KWH	First 1000 KWH -	0.1156 P/KWH
Over 200 KWH -	0.0741 P/KWH	Over 1000 KWH -	0.0974 P/KWH

The Fuel Escalator Adjustment for January 1982 for both Residential and Commercial rates is $0.060427 X KWH.

Also there is a correlation in the increased utilization of electricity due to increases in lighting for safety and security of our residents, and for the recreational facilities that are used at night contribute towards increasing this cost.

The electricity charges here in the Virgin Islands are higher than any throughout the Nation. The projected 1982 electricity cost of $372,000 already mentioned is for the Authority's "in-house" operation only. When these same rates are applied to the Utility Allowance Schedule, the Authority is faced with a perilous financial situation.

Residents pay for electricity and gas which are considered in the following utility allowance which is deducted from the gross rent. It should be noted that the schedule was revised in 1980 and will increase drastically when the new Federal Policy relative to the method by which a PHA determines tenant utility allowance amounts is adopted by this Authority in the near future. The 1981 revision was held in abeyance until the new regulations were issued by HUD.

Conventional Low-Rent Public Housing - Virgin Islands
Allowance for Tenant - Furnished Utilities
Total Monthly Allowances
(All Totals Include General Purpose Electric)

No. of Bedrooms	Electric Cooking with Water Heater	Elec. Cooking without Water Heater	Gas Cooking with Water Heater	Gas Cooking without Water Heater
0-BR	$ 35.00	$ 25.00	$ 34.00	$ 24.00
1-BR	46.00	33.00	45.00	32.00
2-BR	58.00	41.00	56.00	39.00
3-BR	69.00	49.00	66.00	46.00
4-BR	87.00	61.00	82.00	56.00
5-BR	98.00	70.00	92.00	64.00

The following data is a sampling of the electrical sampling (gas not included) for the first six months of 1981 for the VIHA Housing Projects on St. Thomas. (The island of St. Croix with the same number of units reflect approximately the same consumption figures.)

ELECTRIC CONSUMPTION DATA
JAN - JUN '81
VIHA PROJECTS

PAUL M. PEARSON/OSWALD HARRIS COURT
(V.I. 1-1) (V.I. 1-5)

Month	Customers Billed	Average KWH/Bill	Total KWH
Jan	481	268	131,052
Feb	481	221	106,301
Mar	484	222	107,448
Apr	491	180	88,380
May	494	210	103,950
Jun	495	217	107,415
Totals	2,934	1,318	644,542
Averages	(489)	(220) $37.66	(107,424)

BERGS HOME
(V.I. 1-4A)

Jan	Based on	246	12,300
Feb	figure of	252	12,600
Mar	50 pro-	221	11,050
Apr	vided by	225	11,250
May	VIHA	445	22,250
Jun		220	11,000
Totals	-	1,609	80,450
Averages	(50)	(268) $44.96	(13,408)

Note: The average monthly electric bill for each project differs because of the bedroom sizes and whether cooking is by gas or electricity.

M.J. KIRWAN TERRACE
(V.I. 1-7)

Month	Customers Billed	Average KWH/Bill	Total KWH
Jan	132	309	40,788
Feb	131	250	32.750
Mar	131	249	32,619
Apr	132	275	36,300
May	132	236	31,152
Jun	132	261	34,452
Totals	790	1,580	208,061
Averages	(132)	(263) $43.87	(34,677)

BERGS HOME ADDITION
(V.I. 1-9)

Jan	Based on	246	5,904
Feb	figure of	252	6,048
Mar	24 pro-	221	5,304
Apr	vided by	225	5,400
May	VIHA	445	10,680
Jun		220	5,280
Totals	-	1,609	38,616
Averages	(24)	(267) $44.44	(6,436)

LUCINDA MILLIN HOME
(V.I. 1-11)

Month	Customers Billed	Average KWH/Bill	Total KWH
Jan	84	230	18,630
Feb	"	102	8,568
Mar	"	90	7,560
Apr	"	90	7,560
May	"	90	7,560
Jun	"	101	8,484
Totals	504	703	58,362
Averages	(84)	(117) $21.48	(9,727)

TUTU HIGH RISE APARTMENTS
(V.I. 1-16)

Jan	Based on	573	229,200
Feb	figure of	353	141,200
Mar	400 pro-	489	195,600
Apr	vided by	401	160,400
May	VIHA	333	133,200
Jun		371	148,400
Totals	-	2,520	1,008,000
Averages	(400)	(420) $66.52	(168,000)

DONOE PROJECT
(V.I. 1-17)

Month	Customers Billed	Average KWH/Bill	Total KWH
Jan	292	518	151,256
Feb	293	364	106,652
Mar	299	338	101,062
Apr	300	411	123,300
May	296	325	96,200
Jun	295	351	103,545
Totals	1776	2,307	682,015
Averages	(296)	(384) $61.32	(113,669)

BOVONI
(V.I. 1-19)

Jan	Based on figure of 364 provided by VIHA	596	216,944
Feb		469	170,716
Mar		491	178,724
Apr		455	165,620
May		477	173,628
Jun		441	160,524
Totals		2,929	1,066,151
Averages	(364)	(488) $76.34	(177,693)

WARREN E. BROWN APARTMENTS
(V.I. 1-26, 27 & 28)

Month	Customers Billed	Average KWH/Bill	Total KWH
Jan	Based on	389	105,808
Feb	figure of	326	88,672
Mar	272 pro-	321	87,312
Apr	vided by	348	94,656
May	VIHA	334	90,848
Jun		330	89,760
Totals		2,048	557,056
Averages	(272)	(341)	(92,843)
		$55.12	

HUD's regulations on computing the utility schedule create disincentives and encourage poor management within PHA's. Utility subsidies are calculated on the basis of the PHA's average consumption over a three-year period and are paid at the current rate.

With this method, there is no need for residents to conserve their usage and no reason for PHA's to initiate conservation measures to save money.

When cubic feet of gas and kilowatt hours are converted to money, especially here in the Virgin Islands, most of the residents' rents are not enough to cover the cost of utilities allowed them under their lease, thereby producing negative rents.

3. The Brooke Amendment

The net effect of the Brooke Amendment has been to reduce the VIHA's income to levels that make solvent operations impossible. The Authority is in favor of repealing this restrictive amendment which would permit us to once again stabilize our fiscal operations and reduce operating subsidies. If we returned to the original concept of the Public Housing Program, that it is not a "give-away" program, rent could be computed on the real income of a family.

This Authority feels, as in the case of many other PHA's across the Nation, that there is further need for the Secretary's Definition of Income to be changed in order for income that now must be excluded to be counted and thereby increase an Authority's revenue. We are in favor of counting Public Assistance Payments, Food Stamps, and Medical Assistance as eligible family income.

Approximately 13% of the Authority's total Public Housing population receive Public Assistance Payments. However, of the total number of families in a negative rent status, 50% of the affected families receive Public Assistance Payments. The Social Welfare System of the Virgin Islands, as in several states, adopted the Consolidated Standard Allowance which provides a flat grant based upon family size with no housing cost identified.

The Brooke Amendment nullifies the provision of the act to allow the Housing Authority to collect a reasonable rent from welfare families. It is important to note also, that the PHA is only allowed to collect rent based on the public assistance payment after adjustments. In reality, the welfare family receives a much larger amount when you consider the welfare payment, food stamps, medical assistance and other benefits.

Although the data on the following pages is somewhat outdated, it is presented to give an indication of the number of persons receiving Public Assistance and Food Stamps. The population of the Virgin Islands during the reporting period was approximately 100,000 people.

V.I. DEPARTMENT OF SOCIAL WELFARE

Division of Income Maintenance

Six Year Comparisons of Monthly Averages of Persons Receiving Public Assistance by Category and Fiscal Year

Category	FYs	1974	1975	1976	1977	1978	1979	% Change**
Federally Subsidized								
Aid to Families with Dependent Children *		4,023	4,111	3,703	3,724	3,326	3,122	(-4.8)
Old Age Assistance		307	291	273	272	255	229	(-5.5)
Aid for the Blind		7	7	7	7	7	7	0
Aid for the Disabled		94	105	136	169	183	182	14.7
Locally Funded								
General Assistance		328	320	318	313	357	359	2.0
Total		4,758	4,835	4,437	4,485	4,128	3,899	(-3.8)
Percent Annual Change			1.5	(-8.2)	1.1	(-8.0)	(-5.5)	(-3.8)

*Includes mothers and children

(**Percent Average Annual Change)

Food Stamp Division

Certified and Participating Households and Individuals by Month and District

Month		Certified Households			Participating Households			
		St. Thomas/ St. John	St. Croix	Total	St. Thomas/ St. John	St. Croix	Total	Total Participating Individuals
1978:	July	6,462	5,318	11,780	2,706	3,473	6,179	26,928
	August	6,546	5,633	12,179	2,653	3,511	6,164	26,880
	September	6,625	6,036	12,661	2,687	3,381	6,068	26,439
	October	6,775	6,304	13,059	2,792	3,326	6,118	26,920
	November	6,830	6,477	13,307	2,744	3,424	6,168	27,295
	December	6,888	6,638	13,526	2,804	3,522	6,326	27,783
1979:	January	7,021	7,041	14,062	3,048	3,586	6,634	28,455
	February	7,044	7,075	14,119	3,137	3,800	6,937	30,201
	March	7,110	7,353	14,463	3,450	4,211	7,661	31,938
	*April	3,588	4,731	8,319	3,464	4,211	7,675	31,618
	May	3,693	4,981	8,674	3,528	4,204	7,732	31,580
	June	3,791	5,175	8,966	3,563	4,305	7,868	32,052
	July	3,858	5,351	9,209	3,622	4,509	8,131	33,267
	August	3,929	5,514	9,443	3,802	4,935	8,737	35,826
	September	4,032	5,652	9,684	3,601	4,792	8,393	34,314
Monthly Average		5,611	6,326	11,563	3,173	3,946	7,119	30,113

*Caseload review: termination of non-participating households

In addition, the total number of individuals in the Virgin Islands receiving medical assistance as of December, 1981 numbered 10,331 broken down as follows:

Welfare recipients	- 3,579
Federal Funded Programs	- 5,222
Local Funded Programs	- 1,530
Total	10,331

It should be noted that during the last two years the figure has dropped drastically from a high of 33,000 individuals in the Medical Assistance Program because the income bracket has not been updated since 1966.

The practice of vendor payments will be pursued by this Authority, whereby the Department of Social Welfare would send the rent payment for a welfare fmaily directly to the Housing Authority. Although it would remove a degree of responsibility from the family, it saves the PHA a significant amount of time, effort, and money in pursuing delinquent rents and in evicting families for non-payment of rent.

Again we recommend that "in-kind income" such as Public Assistance Payments, Food Stamps, and Medical Assistance Payments be used as a part of the gross income in computation of rent.

4. Negative Rents

The Virgin Islands Housing Authority in accordance with guidelines issued by HUD, revised its utility allowance schedule in 1976 for the first time in ten years. With the impact of this new schedule, zero and negative rentals first appeared.

Zero and negative rentals occur in low-income families when the allowance for utilities exceeds the gross rent. The family pays no rent and receives a credit for the excess. In 1980, the Authority was mandated by HUD to make monthly payments to families in this status. In 1981 1,058 families were in a negative status and the Authority paid out $291,881 in utility refunds.

In accordance with HUD's recommendations and VIHA Board Resolution, the Authority revised its Utility Allowance again in 1980 which reflected an increase of seventy-five percent (75%). Early in 1982, we will once again revise our Utility Schedule with further allowances.

The projection of the Management Operating Budget request for 1982 reflects anticipated income from dwelling rental of $3,435,820 less losses from negative dwelling rental of $137,880. The projected net dwelling rental for 1982 of $3,297,940 represents an increase of $272,310 over the expected dwelling rental for 1981 of $3,025,630.

The 1982 projection represents a nine percent (9%) increase over 1981 anticipated dwelling rental. The increase is attributed to changes in rent rates, retroactive re-examination of residents and the resident turn-over rates (i.e. families of higher income being placed in accordance with Resolution No. 928, Financial Solvency Criteria, effective October 4, 1978.)

In addition, in compliance with Low-Rent Housing Accounting Handbook HM 7510.01, Chapter 13, Section 12, and with HUD's letter dated October 10, 1979, re "Payments to families with Negative Rents", the

Authority will be required to disburse at least $11,490 monthly to approximately 645 families in 1982, according to our projection. The effect of this monthly disbursement and increase in expenditures will have a negative impact on the Authority's cash flow. It is anticipated that approximately $137,880 will be incurred as Dwelling Rental Negative Loss for 1982. The average Dwelling Rental Negative Loss is currently $17.81 per negative rent.

The interim rule implements the provisions of the United States Housing Act of 1937 as amended by the Housing and Community Act of 1974 that are applicable to rents to be charged residents in low-income housing communities. The Housing and Community Act of 1974 restricted rents to be charged public housing residents to one-fourth (25%) of the family's income; however, with the passage of the new regulations allowing a 5% increase to 30% of adjusted income, the negative rent situation should start to show improvement, but only if the full 5% adjustment is applied in 1982 and not 1% over the next five years.

We are disturbed by the concept of negative rents. How are we to encourage residents to become fiscally responsible if through utility reimbursement they are being paid to live in public housing? Negative rents amount to "hand-holding," which is counterproductive to developing initiative and independence.

It is our recommendation that no future policy should be created which provides for less than a minimum rent of approximately $25.00 per month per unit.

It is inconceivable that the Federal government would place itself in a position to provide living accommodations to anyone at no cost.

5. Permanent/Bonded Alien Population Residing in VIHA Housing Communities

Over seventy-five percent (75%) of the Public Housing Population residing in VIHA administered communities are made up of either permanent or bonded aliens. At the outset, we would like to state that the Authority's position on immigration is a positive one; however, it does pose problems when a local Virgin Islander has to wait, sometimes for years, for admission into the Public Housing Program because of inavailability of units.

We abide by Executive Order 11063, Equal Opportunity in Housing, which directs Federal departments and agencies to take all action necessary and appropriate to prevent discrimination because of race, color, creed, or national origin in the sale, leasing, rental, or other disposition of residential property and related facilities which are owned or operated by the Federal government or provided with Federal assistance.

The Authority feels that migration of non-citizens to the Virgin Islands must be aligned to the ability of this Territory to absorb immigrants in the areas of not only housing, but employment, education, and public assistance as well.

Consider the effects on rental income when a mother or father or both receive permanent status; then because of a change in the immigration quota, they bring in their children from a newly emerged

Caribbean Nation. Not only does the unit become overcrowded, but each child reduces the gross income of that family, thereby reducing the rent we can charge.

The 1981 legislative changes in the federal housing programs are contained in Title III, Subtitle A of the Omnibus Reconciliation Act of 1981, which may also be cited as the Housing and Community Development Amendments of 1981. The Act is Public Law 97-35; and was signed into law August 13, 1981, with an effective date of October 1, 1981.

The Act contains a provision prohibiting assistance under the public housing, Section 8, Section 235, 236 or Rent Supplemental programs to an alien unless the alien is a resident of the United States and either is lawfully admitted for permanent residence as an immigrant (excluding visitors, tourists, diplomats, and students who enter the United States temporarily with no intention of abandoning their residence in a foreign country); entered prior to June 30, 1948, has continuously maintained residence in the United States, is not eligible for citizenship, but is deemed to be lawfully admitted for permanent residence as a result of an exercise of discretion by the Attorney General; is lawfully present and granted asylum; is lawfully present because permitted by the Attorney General for strictly public interest or emergency reasons; or is lawfully present because deportation is withheld by the Attorney General.

In regard to invasion of privacy questions, the Authority feels that it is not the intention of the bill to authorize the Secretary of Housing and Urban Development or any other public official to invade the privacy of occupants of assisted housing in an effort to identify illegal aliens and to secure their removal.

However, the Secretary should take reasonable steps to identify such persons by methods which may include a request for documentation of an occupant's legal status. The Secretary should also take steps to provide for an orderly transition which will satisfy the intent of the proposal to make assisted housing available to lawful residents exclusively.

In undertaking this task, the Secretary should ensure that persons administering assisted housing programs deal fairly and humanly with all persons discovered to be occupying housing in violation of this section.

In establishing procedures to assure that future applicants for participation in assisted housing programs are persons lawfully present in the Territory of the Virgin Islands, the Secretary should assure that all applicants are subjected to procedures which are fair but at the same time give a PHA the legal authority to determine whether a particular applicant is in fact lawfully present in the United States or its Territories.

SUMMARY

This paper looks at the Virgin Islands Public Housing Program as it exists currently and brings into focus some of the major issues confronting it.

There are many complex problems that are responsible for the state of Public Housing throughout the Nation and many others that apply only here in the U.S. Virgin Islands.

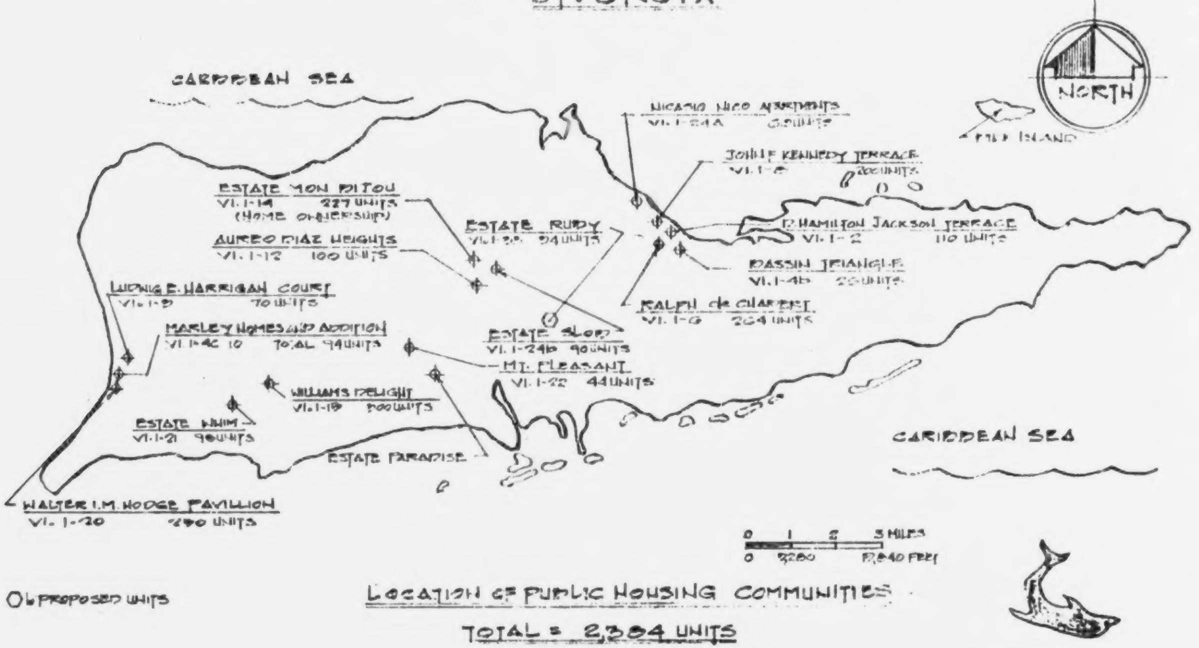
Exclusion from the Performance Funding System; an inequitable inflation factor in granting subsidies; the highest electric rates in the Nation; lack of an identified housing cost in the Social Welfare System; the concept of negative rents; the large percentage of Permanent/Bonded Aliens making up our resident population are to name just a few.

A gradual lessening of the PHA's dependency on subsidy should be the primary goal of HUD and PHA's alike, and the discussion of the issues in this paper leads to that direction. There is also a need for change in legislation, namely repeal of the outdated Brooke Amendment, so we can once again return to a solvent fiscal PHA operation.

Clearly, not all the issues involved in the Virgin Islands Public Housing Program have been raised, and of those discussed, none have been discussed in detail. It is the intent of this paper to present a compact, focused statement to establish an overall picture of our Public Housing Program and suggestions for improving it.

We are anxious that Congress which writes Housing legislation be aware of our concerns and ideas to help alleviate the situation and we stand ready to assist in the further exploration of these issues and a formulation of strategy for realizing the improvement.

VIRGIN ISLANDS HOUSING AUTHORITY
ST. CROIX


CARIBBEAN SEA
NORTH
BUCK ISLAND
NICASIO NICO APARTMENTS
VI. 1-24A 60 UNITS
JOHN F. KENNEDY TERRACE
VI. 1-8 200 UNITS
ESTATE MON BIJOU
VI. 1-14 227 UNITS
(HOME OWNERSHIP)
ESTATE RUBY
VI. 1-30 94 UNITS
D. HAMILTON JACKSON TERRACE
VI. 1-2 110 UNITS
AUREO DIAZ HEIGHTS
VI. 1-12 100 UNITS
BASSIN TRIANGLE
VI. 1-4B 20 UNITS
LUDWIG E. HARRIGAN COURT
VI. 1-9 70 UNITS
RALPH de CHABERT
VI. 1-6 264 UNITS
MARLEY HOMES AND ADDITION
VI. 1-4C 10 TOTAL 94 UNITS
ESTATE SLOB
VI. 1-24B 90 UNITS
MT. PLEASANT
VI. 1-22 44 UNITS
WILLIAMS DELIGHT
VI. 1-19 300 UNITS
ESTATE WHIM
VI. 1-21 90 UNITS
ESTATE PARADISE
CARIBBEAN SEA
WALTER I.M. HODGE PAVILLION
VI. 1-20 250 UNITS
0 1 2 3 MILES
0 5280 15,840 FEET

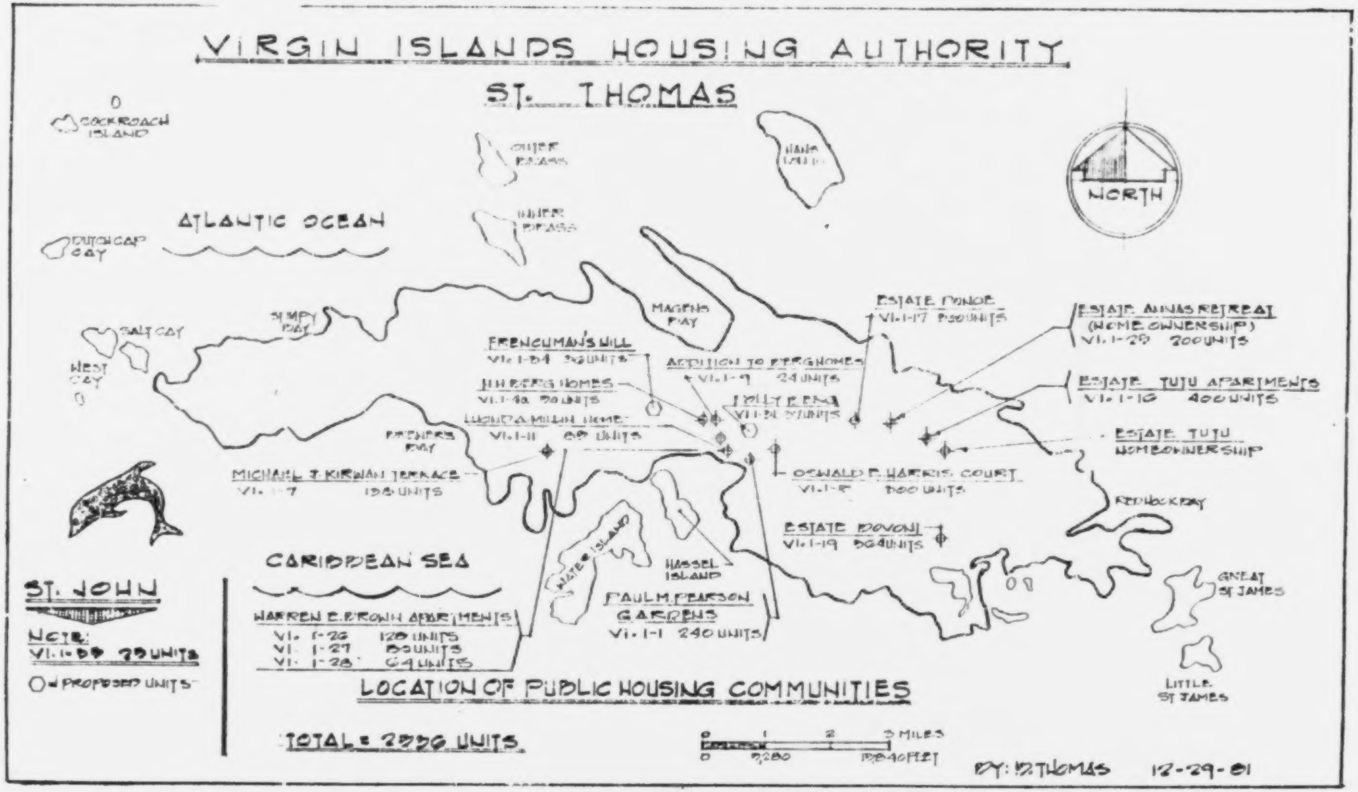
O = PROPOSED UNITS

LOCATION OF PUBLIC HOUSING COMMUNITIES

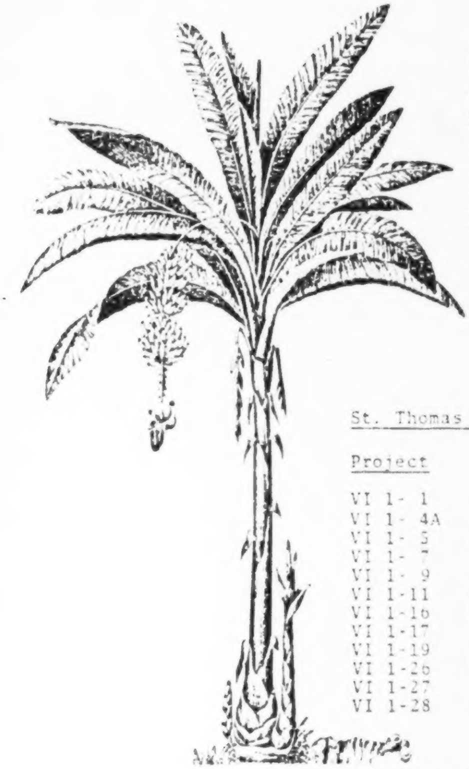
TOTAL = 2,304 UNITS

BY: R. THOMAS 12-28-81

1480


VIRGIN ISLANDS HOUSING AUTHORITY
ST. THOMAS
COCKROACH ISLAND
OUTER BRASS
INNER BRASS
HANS LOLLIK
NORTH
ATLANTIC OCEAN
DUTCHCAP CAY
SALT CAY
WEST CAY
SIMPSON BAY
MAGENS BAY
FRENCHMAN'S HILL
VI. 1-34 32 UNITS
H.H. BERG HOMES
VI. 1-4a 70 UNITS
LUCINDA MILLIN HOME
VI. 1-11 69 UNITS
ADDITION TO BERG HOMES
VI. 1-9 24 UNITS
EMILY E. ...
VI. 1-31 ... UNITS
ESTATE DONOE
VI. 1-17 250 UNITS
ESTATE ANNAS RETREAT
(HOME OWNERSHIP)
VI. 1-29 300 UNITS
ESTATE TUTU APARTMENTS
VI. 1-16 400 UNITS
ESTATE TUTU
HOMEOWNERSHIP
BREWERS BAY
MICHAEL J. KIRWAN TERRACE
VI. 1-7 138 UNITS
OSWALD E. HARRIS COURT
VI. 1-5 300 UNITS
ESTATE BOVONI
VI. 1-19 364 UNITS
RED HOOK BAY
GREAT ST. JAMES
LITTLE ST. JAMES
WATER ISLAND
HASSEL ISLAND
CARIBBEAN SEA
WARREN E. BROWN APARTMENTS
VI. 1-26 128 UNITS
VI. 1-27 80 UNITS
VI. 1-28 64 UNITS
PAUL M. PEARSON GARDENS
VI. 1-1 240 UNITS
ST. JOHN
NOTE:
VI. 1-33 75 UNITS
○ = PROPOSED UNITS
LOCATION OF PUBLIC HOUSING COMMUNITIES
TOTAL = 2556 UNITS
0 1 2 3 MILES
0 5280 15840 FEET
BY: B. THOMAS 12-29-81

1481



PHA-Owned Rental Housing

The Virgin Islands Housing Authority presently has 4,329 units of conventional low-rent housing. Of this total, twelve (12) communities consisting of 2,173 units are located in St. Thomas and sixteen (16) communities consisting of 2,156 are located in St. Croix.

St. Thomas Housing Communities

Project		Total No. of Units
VI 1- 1	Paul M. Pearson Gardens	240
VI 1- 4A	H. H. Berg Homes	50
VI 1- 5	Oswald E. Harris Court	300
VI 1- 7	Michael J. Kirwan Terrace	138
VI 1- 9	Addition to Berg Homes	24
VI 1-11	Lucinda A. Millin Home	85
VI 1-16	Estate Tutu Apartments	400
VI 1-17	Estate Donoe	300
VI 1-19	Estate Bovoni	364
VI 1-26	Warren E. Brown I	128
VI 1-27	Warren E. Brown II	80
VI 1-28	Warren E. Brown III	64
	Total	2,173

St. Croix Housing Communities

VI 1- 2	D. Hamilton Jackson Terrace	110
VI 1- 3	Ludvig E. Harrigan Court	70
VI 1- 4B	Bassin Triangle	26
VI 1- 4C	Marley Homes	34
VI 1- 6	Ralph de Chabert Place	264
VI 1- 8	John F. Kennedy Terrace	200
VI 1-10	Addition to Marley Homes	60
VI 1-12	Aureo Diaz Heights	100
VI 1-15	William's Delight	300
VI 1-18	Louis E. Brown Villas	256
VI 1-20	Walter I.M. Hodge Pavillion	250
VI 1-21	Whim Gardens	100
VI 1-22	Mount Pleasant	44
VI 1-23	Louis E. Brown Villas	192
VI 1-24A	Nicasio Nico Apartments	60
VI 1-24B	Estate Slob	90
	Total	2,156

BEST DOCUMENT AVAILABLE

VIRGIN ISLANDS HOUSING AUTHORITY

PHA-OWNED RENTAL HOUSING
DECEMBER 1981 MONTHLY DWELLING RENTAL